



**COMMONWEALTH OF PUERTO RICO**

Comprehensive Annual Financial Report

Fiscal Year Ended June 30, 2003

# **COMPREHENSIVE ANNUAL FINANCIAL REPORT**

*Fiscal Year Ended June 30, 2003*



***Commonwealth of Puerto Rico***

***Honorable Sila María Calderón***

***Governor***

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***Puerto Rico Department of the Treasury***

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*This document is available on the Puerto Rico Department of the Treasury homepage*

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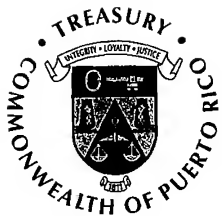
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## **INTRODUCTORY SECTION**



Juan A. Flores Galarza, CPA  
Secretary

June 9, 2004

To the Honorable Governor of Puerto Rico,  
Members of the Legislature, and People of Puerto Rico:

It is a pleasure to submit, for your information, the Comprehensive Annual Financial Report (CAFR) of the Commonwealth of Puerto Rico (the Commonwealth) as of and for the fiscal year ended June 30, 2003. This report, presented in three sections, Introductory, Financial, and Statistical, is the primary means of reporting the Commonwealth's financial activities.

The introductory section, which is not audited, includes this letter of transmittal, general information about the Commonwealth, a list of the Commonwealth's principal elected and appointed officials, an organizational chart, and a reproduction of the Certificate of Achievement for Excellence in Financial Reporting that the Commonwealth received for its June 30, 2002 CAFR. The Financial Section contains the independent auditors' report, management's discussion and analysis (MD&A), and the basic financial statements as listed in the table of contents. The financial section also includes the notes to the basic financial statements, required supplementary information, and other supplementary information. The statistical section, which is not audited, includes selected financial and demographic information, generally presented on a multi-year basis.

### **PROFILE OF THE COMMONWEALTH**

The Puerto Rico Department of the Treasury is responsible for the preparation of this report. The responsibility for the accuracy of presented data and the completeness and fairness of the presentation, including all of the disclosures, rests on the Commonwealth's management. To the best of our knowledge and belief, the following data, as presented, is accurate in all material respects, and is presented in a manner designed to set forth the financial position and the results of operations of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth as of June 30, 2003 and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America. We have included all the necessary disclosures to enable the reader to gain a thorough understanding of the Commonwealth's activities.

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The financial reporting entity includes all funds of the Commonwealth, which is the primary government, as well as all its component units. In accordance with Governmental Accounting Standards Board Statement No. 14, the Commonwealth's financial reporting entity includes 48 component units; 6 are blended component units including 3 fiduciary component units, 7 major discretely presented component units, and 35 nonmajor discretely presented component units. Component units are legally separate entities for which the primary government is financially accountable, or other organizations, the nature and significance of whose relationship with the Commonwealth are such that exclusion would cause the Commonwealth's basic financial statements to be misleading and incomplete. Blended component units, although legally separate entities, are, in substance, part of the primary government's operations and are included as part of the primary government. Discretely presented component units, both major and nonmajor, are reported in a separate column in the government-wide financial statements to emphasize that they are not part of the primary government and to differentiate their financial position and results of operations from those of the primary government.

Generally, each component unit issues audited financial statements, which can be obtained from the component unit's administrative offices. The basic financial statements included in the financial section of this CAFR provide descriptions of the operations of each of the following component units of the Commonwealth:

*Blended Component Units:*

Public Buildings Authority  
Puerto Rico Maritime Shipping Authority  
The Children's Trust

*Discretely Presented Component Units:*

Agricultural Services and Development Administration  
Automobile Accident Compensation Administration  
Caribbean Basin Projects Financing Authority  
Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico  
Economic Development Bank for Puerto Rico  
Employment and Training Enterprises Corporation  
Farm Insurance Corporation of Puerto Rico  
Fine Arts Center Corporation  
Governing Board of the 9-1-1 Service  
Government Development Bank for Puerto Rico  
Land Authority of Puerto Rico  
Musical Arts Corporation  
National Parks Company of Puerto Rico  
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives

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Puerto Rico Aqueduct and Sewer Authority  
Puerto Rico and Caribbean Cardiovascular Center Corporation  
Puerto Rico Conservatory of Music Corporation  
Puerto Rico Convention Center District Authority  
Puerto Rico Council on Higher Education  
Puerto Rico Electric Power Authority  
Puerto Rico Exports Development Corporation  
Puerto Rico Government Investment Trust Fund  
Puerto Rico Health Insurance Administration  
Puerto Rico Highway and Transportation Authority  
Puerto Rico Industrial Development Company  
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities  
Financing Authority  
Puerto Rico Infrastructure Financing Authority  
Puerto Rico Land Administration  
Puerto Rico Maritime Transportation Authority  
Puerto Rico Medical Services Administration  
Puerto Rico Metropolitan Bus Authority  
Puerto Rico Municipal Finance Agency  
Puerto Rico Ports Authority  
Puerto Rico Public Broadcasting Corporation  
Puerto Rico School of Plastic Arts  
Puerto Rico Solid Waste Authority  
Puerto Rico Telephone Authority  
Right to Employment Administration  
Special Communities Perpetual Trust  
State Insurance Fund Corporation  
Tourism Company of Puerto Rico  
University of Puerto Rico

*Fiduciary Component Units:*

Employees Retirement System of the Government of Puerto Rico and its Instrumentalities  
Puerto Rico Judiciary Retirement System  
Puerto Rico System of Annuities and Pensions for Teachers

**Independent Auditors**

Commonwealth statutes require an annual audit by independent certified public accountants. The firm of KPMG LLP was selected by the Commonwealth to perform the audit of the basic financial statements in accordance with auditing standards generally accepted in the United States of America for the fiscal year



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2002-2003. The goal of the independent audit was to provide reasonable assurance that the financial statements of the Commonwealth for the fiscal year ended June 30, 2003, are free of material misstatements. The independent auditor's report on the basic financial statements is included in the financial section of this report.

### **Internal Controls**

The management of the Commonwealth is responsible for establishing and maintaining internal controls to ensure that assets of the Commonwealth are protected from loss, theft, or misuse, and that adequate accounting data is compiled for the preparation of financial statements in conformity with accounting principles generally accepted in the United States of America. The internal controls are designed to provide reasonable, but not absolute, assurance that these objectives are met. The concept of reasonable assurance recognizes that: (1) the cost of a control should not exceed the benefits likely to be derived; (2) the valuation of costs and benefits requires estimates and judgments by management.

As a recipient of federal assistance, the Commonwealth is also responsible for ensuring that internal controls are in place to ensure that documents and processes are in compliance with applicable laws and regulations related to such federal financial assistance programs.

Certain departments, agencies, and political subdivisions are subject to the requirements of the U.S. Office of Management and Budget Circular A-133. As a result, these entities are audited for compliance with the requirements of the federal financial assistance programs. These audits are performed at the department or agency level. The Commonwealth has provided for the possible cost disallowance that may arise from these audits, as well as from other audits that may be performed by federal grantors.

### **Budget and Fiscal Policy**

The fiscal year of the Commonwealth begins each July 1. The Governor is constitutionally required to submit to the Legislature an annual balanced budget of capital improvements and operating expenses of the Central Government for the ensuing fiscal year.

The annual budget is prepared by the Puerto Rico Office of Management and Budget, working with the Planning Board, the Puerto Rico Department of the Treasury, and other government offices and agencies. Section 7 of Article 6 of the Constitution provides that *"The appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."*

The Commonwealth maintains extensive budgetary controls. The objective of these controls is to ensure compliance with legal provisions embodied in the annual appropriated budget approved by the Legislature. Activities of the general fund are included in the annual appropriated budget. Budgetary control resides at the

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department level. The Commonwealth also maintains an encumbrance accounting system as one method of maintaining budgetary control.

The annual budget, which is developed using elements of performance-based program budgeting and zero-based budgeting, includes an estimate of revenue and other resources for the ensuing fiscal year under laws existing at the time the budget is submitted and legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in her judgment are necessary, convenient and in conformity with the four-year investment plan prepared by the Planning Board.

The Legislature may amend the budget submitted by the Governor, but may not increase items that would cause a deficit without imposing additional taxes to cover such deficit. Once approved by the Legislature, the budget is referred to the Governor, who may decrease or eliminate any item, but may not increase or insert new items in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature with her objections. The Legislature, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, as originally approved by the Legislature and the Governor, it is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This allows the Commonwealth to continue to pay its operating and other expenses until a new budget is approved.

### **Governmental Activities**

General governmental activities are accounted for in four governmental funds. These funds are: general, special revenue, debt service, and capital project. The general fund is the primary operating fund of the Commonwealth. The general fund is used to account for resources traditionally associated with government, which are not required legally or by sound financial management to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, education and economic development. Other major funds are the debt service fund, which accounts for the accumulation of resources predominantly for, and the payment of the Commonwealth general long-term bonds' principal, interest and related costs, the Public Building Authority capital project fund, which accounts for the financial resources used for the acquisition and construction of major capital facilities and The Children's Trust special revenue fund which accounts for the moneys received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The financial resources received by this fund are used to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico. Nonmajor governmental funds are combined in a single column in the governmental fund financial statements, and individually identified in the supplementary combining nonmajor governmental funds financial statements of this report.



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### **Business-Type Activities**

Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises, where the intent of the government is that the costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges or where the government has decided that periodic determination of net income is appropriate for accountability purposes.

The Commonwealth's proprietary operations comprise the following activities: the unemployment insurance trust fund, and the Lottery of Puerto Rico and the Additional Lottery System (the Lotteries Fund), both major funds. The Puerto Rico Water Pollution Control Revolving Fund, the Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund, the Disability Insurance Fund, and the Drivers' Insurance Fund are all nonmajor proprietary funds combined in a single column in the proprietary fund financial statements, and individually identified in the supplementary combining nonmajor proprietary funds financial statements of this report.

### **Fiduciary Operations**

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity or as an agent for individuals, private organizations, and other governmental units. These include the pension trust and agency funds. Pension trust funds are established through trust agreements specifying how the fund will operate. Agency funds are custodial in nature and do not report fund balances. The pension trust funds include the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities, the Puerto Rico Judiciary Retirement System, and the Puerto Rico System of Annuities and Pensions for Teachers.

Agency funds consists of the Special Deposits Fund. This agency fund includes deposits under the custody of the Courts of Justice for alimony payments, deposits under the custody of the Insurance Commissioner for escheated property, and for insurance companies under bankruptcy.

### **Cash Management Policies and Practices**

The Commonwealth maintains a cash pool for its cash and cash equivalents. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing accounts in the Government Development Bank for Puerto Rico (GDB), a discretely presented component unit. In addition, the Puerto Rico Government Investment Trust Fund (PRGITF), was created by the Commonwealth pursuant to Act No. 176 of August 11, 1995, and began operations on December 4, 1995. PRGITF is a no-load diversified collective investment trust that was created for the purpose of providing eligible investors with a convenient and economical way to invest in a professionally managed money market portfolio. The deposits on hand and the investments purchased are not collateralized, secured, or guaranteed by the Commonwealth or any of its agencies, instrumentalities, or political subdivisions.

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The Commonwealth's investment policy is to minimize credit and market risk while maintaining a competitive yield on its portfolio. The cash temporarily idle during this year was invested mainly in U.S. government securities, stocks, corporate bonds, repurchase agreements, Commonwealth securities, trading securities, and short-term investments. These are primary government investments that are restricted and unrestricted.

### **Capital Assets**

These basic financial statements include the capital assets of the Commonwealth. A discussion of capital assets accounting is included in the Management's Discussion and Analysis that is part of the basic financial statements. More detailed information about capital assets can be found in the notes to the basic financial statements.

### **Debt Administration**

As of June 30, 2003, the Commonwealth had a number of debt issues outstanding. The Commonwealth has maintained an A- credit rating from Standard and Poor's Corporation and a Baal from Moody's Investor Service on general obligation bond issues, and we expect that these classifications will be maintained or improved in future years.

The Constitution of the Commonwealth limits the amount of debt service that can be incurred with respect to issued or guaranteed debt to 15% of internal revenue, as therein defined. As of June 30, 2003, the Commonwealth is in compliance with the debt limitation requirement. See the computation of the Legal Debt Margin on page 3 in the Statistical Section. More detailed information about long-term debt can be found in the notes to the basic financial statements.

### **Risk Financing**

The Commonwealth purchases commercial insurance to cover casualty, theft, tort claims, and other losses. The current insurance policies have not been canceled or terminated. As it relates to Worker's Compensation, the Commonwealth's discretely presented component unit, the State Insurance Fund Corporation, provides workers' compensation to both public and private employees.

### **Financial Advisor and Fiscal Agent**

The principal functions of GDB are to act as financial advisor to and fiscal agent for the Commonwealth, its municipalities, and public corporations, in connection with the issuance of bonds and notes, and to make loans to private enterprises to aid the economic development of Puerto Rico.



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GDB was the first governmental entity in Puerto Rico to obtain a Certificate of Achievement for Excellence in Financial Reporting for its CAFR. It has received the award for the years ended June 30, 1994 through 2002. GDB is presented as a major discretely presented component unit.

### **ECONOMIC CONDITIONS AND OUTLOOK**

Puerto Rico enjoyed almost two decades of economic expansion through fiscal year 2001. Almost every sector of the economy participated, and record levels of employment were achieved. Factors behind this expansion included government-sponsored economic development programs, periodic declines in the value of the U.S. dollar, which is the currency used in the Commonwealth, increases in the level of federal transfers, a significant expansion in construction investment driven by infrastructure projects and private investment, primarily in housing, the relatively low cost of borrowing, and low oil prices.

Puerto Rico has a diversified economy with manufacturing and services comprising its principal sectors. The economy of Puerto Rico is closely linked to the United States economy. The following exogenous variables are affected by the United States economy: exports, direct investment, transfer payments, interest rates, inflation, and tourist expenditures. During fiscal year 2003 (July 2002 through June 2003), approximately 86% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 49% of Puerto Rico's imports. In fiscal year 2003, Puerto Rico experienced a \$21.4 billion positive merchandise trade balance.

Puerto Rico has a diversified economy with manufacturing and services comprising its principal sectors. Manufacturing is the largest sector in terms of gross domestic product. The Planning Board estimates that in fiscal year 2003 manufacturing generated \$31.3 billion, or 42.0%, of gross domestic product, as compared with fiscal year 2002 when it generated \$30.0 billion, or 42.2%, of gross domestic product. Manufacturing in Puerto Rico is now more diversified than during the earlier phases of its industrial development and includes several industries less prone to business cycles. In the last three decades, industrial development has tended to be more capital intensive and more dependent on skilled labor.

The services sector, which includes finance, insurance, real estate, wholesale and retail trade, tourism, and other services generated \$28.7 billion, or 38.63%, of Puerto Rico's gross domestic product in fiscal year 2003, as compared with \$27.2 billion, or 38.2%, of gross domestic product in fiscal year 2002. The development of the services sector has shown a strong interaction with manufacturing, tourism, construction, and agriculture.

Tourism makes a significant contribution to economic activity. Total visitors' expenditures accounted for 3.6% of the island's gross domestic product in fiscal year 2003. An estimated 4.4 million visitors spent \$2.7 billion in Puerto Rico in fiscal year 2003. San Juan has become the largest home port for cruise ships in the Caribbean and the fourth largest home port for cruise ships in the world. During the year 2003, the number of persons registered in tourist hotels increased 8.6% in comparison with fiscal year 2002, when tourism was adversely affected by 9/11.

The construction sector contributed to the economic activity from fiscal year 1999 through fiscal year 2003. During that period, construction investment decreased 3.1%. Puerto Rico is heavily dependent on oil imports for the production of electricity. As a result of the construction of two cogeneration plants, however, one of which is fueled by liquefied natural gas and the other by coal, Puerto Rico's dependence on oil imports for the production of electricity has been reduced from 99% to 72%.

The Planning Board's preliminary reports of the performance of the Puerto Rico economy during fiscal year 2003 indicate that the economy registered an increase of 5.2% in total gross product. Gross product in fiscal year 1999 was \$38.3 billion and gross product in fiscal year 2003 was \$47.4. This represents an increase in gross product of 23.76% from fiscal year 1999 to fiscal year 2003.

In terms of personal income, in fiscal year 2003, aggregate personal income was \$43.6 billion (\$41.7 billion in 2000 prices) and personal income per capita was \$11,279 (\$10,784 in 2000 prices).

According to the Department of Labor and Human Resources Household Employment Survey, during fiscal year 2003, total monthly employment averaged 1,210,800 compared to 1,158,000 in fiscal year 2001. Notwithstanding the increase in average monthly employment, due to a higher labor participation rate and a significant increase in the civilian population aged 16 years and over, the unemployment rate increased from 12.0% during fiscal year 2002 to 12.1% in fiscal year 2003.

## **Major Initiatives**

### ***Individual Income Taxes***

Resident individuals are subject to tax on their taxable income from all sources. As a result of legislation enacted in 1999 and 2000, there are several changes in income tax brackets applicable to future taxable years. However, due to significant limitation of available resources, the Commonwealth has deferred further reduction in income tax rates through fiscal year 2004, in an effort to maintain revenue levels, and avoid budgetary shortfalls. On April 11, 2001, the Commonwealth approved legislation to reduce capital gain tax rate from 20% to 10%.

### ***Industrial Incentives Program***

#### ***Sections 30A and 936 of the U.S. Internal Revenue Code***

For many years, U.S. companies operating in Puerto Rico enjoyed a special tax credit that was available under Section 936 of the U.S. Internal Revenue Code. Originally, the credit provided an effective 100% federal income tax exemption for most operating income, as well as qualifying investment income from Puerto Rico sources. Amendments to Section 936 made in 1993 (the 1993 Amendments) instituted certain methods for calculating the tax credit and limited the amount of the credit that a qualifying company can claim. As a result of amendments incorporated in the Small Business Job Protection Act of 1996, (the 1996 Amendments), the tax credit is now being phased-out over a 10-year period for existing 936 credit claimants



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and is no longer available for corporations that established operations in Puerto Rico after October 13, 1995 (including existing 936 Corporations, if they establish new product lines in Puerto Rico). The 1996 Amendments also moved the credit based on the economic activity limitation to Section 30A of the Code and phased it out over 10 years. In addition, the 1996 Amendments eliminated the credit previously available for income derived from certain qualified investments in Puerto Rico.

Because of the credit limitations and impending phase-out of Sections 30A and 936, a large number of entities previously operating under the provisions of those sections have restructured their operations in Puerto Rico, in whole or in part, to become controlled foreign corporations (CFC). The Puerto Rico Office of Tax Exemption has received notification of over 60 corporations that have converted part or all of their operations under Puerto Rico tax incentives laws to CFCs. These include most major pharmaceutical, instrument, and electronics manufacturing companies in Puerto Rico. CFCs operate under transfer pricing rules for intangible income that are different from those corporations operating under Sections 30A and 936. In many cases, they are allowed to attribute a larger share of this income to their Puerto Rico operations, but must make a royalty payment "commensurate with income" to their U.S. affiliates. Section 936 companies were exempted from Puerto Rico withholding taxes on any cost-sharing payments they might have opted to make, but CFCs are subject to a 10% Puerto Rico withholding tax on royalty payments.

#### *Proposed New U.S. Tax Regime for Companies Doing Business in Puerto Rico*

In order to enhance the attractiveness for U.S. companies of establishing operations in Puerto Rico, the Commonwealth has been seeking to provide for a new and permanent tax regime applicable to U.S.-based businesses that have operations in the Commonwealth or other U.S. possessions. During the past three years, the Commonwealth has been pursuing an amendment to Section 956 of the United States Internal Revenue Code of 1986, as amended (the Code), that would establish a regime based on the tax rules generally applied to U.S. companies with international operations, but with certain modifications intended to promote employment both in the Commonwealth and the United States. The U.S. Congress, however, has not acted upon the proposed amendment to Section 956 of the Code. Also, due to the phase-out of Sections 30A and 936 of the Code, the U.S. Senate designated a special commission through the General Accounting Office to study the economic impact of said phase-out and to present recommendations on alternative tax incentives for U.S.-based companies operating in Puerto Rico. In the meantime, most U.S.-based companies operating under Sections 30A and 936 of the Code have converted from U.S. corporations to Puerto Rico or foreign corporations, which has lessened the impact of the phase-out of those sections.

#### *Public Sector Debt*

Historically, the Commonwealth has maintained, as a matter of fiscal policy, a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. During certain fiscal years, however, public sector debt increased at a greater rate than the rate of gross product primarily due to an increase in the amount of debt incurred to finance certain key infrastructure projects,

which are important to the development of the economy and are expected to produce long-term economic benefits, and debt incurred to refinance outstanding debt to enable Puerto Rico to benefit from the historically low levels of interest rates and realize debt service savings. During fiscal year 2003, public sector debt increased 6.1%, compared to a 5.2% increase in gross product for the same fiscal year.

### *Prospects for the Future*

The Commonwealth is committed to research and pursue solutions to improve the Commonwealth's competitive economic performance and the quality of life for its citizens. The Governor of Puerto Rico has established three long-range priorities which she expressed in her February 2002 state message. Those priorities, named "El Proyecto Puertorriqueño para el Siglo XXI", are: (1) to provide the Commonwealth a clean and corruption-free government, (2) to establish and promote an economic development program and to fight for the citizens' employments, and (3) to establish a government that works for the family and its working members.

The Commonwealth's economic development program is based on the fundamental, interrelated changes in technology, demographics, and institutions, which are transforming the global economy. These changes provide the challenges and opportunities that encompass the economic development strategy.

The economic program is based on: (1) jump-starting the manufacturing sector, (2) regionalizing (decentralizing) economic development planning and implementation, and (3) "Operación Manos Tecnológicas" to enable industries to acquire and develop more advanced technologies.

Initiatives to achieve the economic development program objectives have begun in the following five areas: (1) legislation towards economic development through tax incentives; (2) institutional development, through economic stimulation through the Puerto Rico Industrial Development Company; (3) new promotional strategies for economic development to build on Puerto Rico's competitive strengths with primary focus on competitive manufacturing clusters in pharmaceutical manufacturing, medical instruments, electronics, and information technology products; (4) refocused strategic projects targeted to include a transshipment port for the South coast of Puerto Rico, and the "Golden Triangle" tourism convention center and world trade complex in San Juan; and (5) federal legislative proposal calling for an amendment to the U.S. Internal Revenue Code of 1986 to provide a new and permanent tax regime applicable to U.S.-based businesses.

### **Financial Condition**

The MD&A, which can be found immediately following the independent auditor's report, provides an overview of the Commonwealth's financial activities addressing both governmental and business-type activities reported in the government-wide financial statements. In addition, the MD&A focuses on the Commonwealth's major funds. Component units and fiduciary activities are excluded from the MD&A.



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### ***Estimated Fiscal Year 2004 Compared to Actual Fiscal Year 2003***

It is projected that the general fund total revenue for fiscal year 2004 will be \$8,295 million, representing an increase of \$441 million, or 5.6%, from actual fiscal year 2003 revenue. The major changes from fiscal year 2003 are expected to be: (1) increases in income taxes from individuals of \$299 million and in corporate income taxes of \$70 million; (2) increases in excise taxes on alcoholic beverages and cigarettes of \$14 million and \$10 million, respectively, motor vehicle excise taxes of \$44 million, and other excise taxes of \$55 million; (3) an increase in electronic lottery of \$32 million; (4) a decrease in miscellaneous nontax revenue of \$146 million; and (5) decreases in taxes on dividends of \$3 million.

### **Other Information**

#### ***Certificate of Achievement***

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a ***Certificate of Achievement for Excellence in Financial Reporting*** to the Commonwealth for its CAFR for the fiscal years ended from June 1996 through 2002. The Certificate of Achievement is a prestigious national award recognizing conformance with the highest standards for the preparation of state and local government financial reports.

In order to be awarded a Certificate of Achievement, a government unit must publish an easily readable and efficiently organized CAFR, whose contents conform to program standards. The CAFR must satisfy both generally accepted accounting principles and applicable legal requirements. A Certificate of Achievement is valid for a period of one year only.

We believe the Comprehensive Annual Financial Report of the Commonwealth as of and for the fiscal year ended June 30, 2003 continues to conform to GFOA standards.

#### ***Acknowledgements***

The preparation of this report requires the collective efforts of numerous finance personnel throughout the Commonwealth and is made possible only with the cooperation and support of the Executive, Legislative, and Judicial branch agencies, universities, and component units of the Commonwealth. We sincerely appreciate the dedicated efforts of all these individuals.

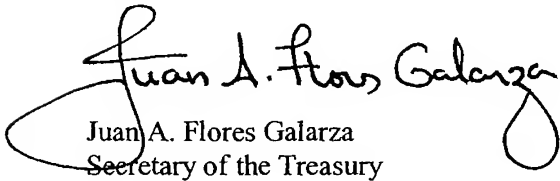
The report could not have been accomplished without the professionalism and dedication of José Alberto Soliván Galio and Miguel Rivera Rivera from our accounting and budget staff as well as the rest of the personnel of the central government accounting area. Also, we would like to give special thanks to our independent auditors, KPMG LLP, for their advice and commitment.

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Honorable Governor of Puerto Rico,  
Members of the Legislature  
and People of Puerto Rico  
June 9, 2004

This report continues our commitment to the citizens of the Commonwealth of Puerto Rico, the Governor, the Legislature, and the financial community, to maintain our general purpose financial statements in conformance with the highest standards of financial accountability.

Respectfully submitted,

  
Juan A. Flores Galarza  
Secretary of the Treasury



SECRETARY OF THE TREASURY



# COMMONWEALTH OF PUERTO RICO

## PRINCIPAL OFFICIALS

**Sila M. Calderón**  
Governor

### Members of the Cabinet

**César Miranda**  
Chief of Staff

**José M. Izquierdo**  
Secretary of State

**Anabelle Rodríguez**  
Secretary of Justice

**Juan A. Flores Galarza**  
Secretary of the Treasury

**César A. Rey**  
Secretary of Education

**Frank Zorrilla Maldonado**  
Secretary of Labor and  
Human Resources

**Johnny V. Rullán**  
Secretary of Health

**Luis Rivero Cubano**  
Secretary of Agriculture

**Fernando E. Fagundo**  
Secretary of Transportation and  
Public Works

**Milton Segarra**  
Secretary of Economic  
Development and Commerce

**Yolanda Zayas Santana**  
Secretary of Family Affairs

**Ileana Echegoyen**  
Secretary of Housing

**Luis E. Rodríguez**  
Secretary of Natural and  
Environmental Resources

**Fernando Torres Ramirez**  
Acting Secretary of  
Consumer Affairs

**Jorge L. Rosario**  
Secretary of Sports and  
Recreation

**Miguel A. Pereira**  
Secretary of Corrections and  
Rehabilitation

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## LEGISLATIVE OFFICERS

**Antonio Fas Alzamora**  
President, Senate

**Carlos Vizcarrondo**  
Speaker, House of  
Representatives

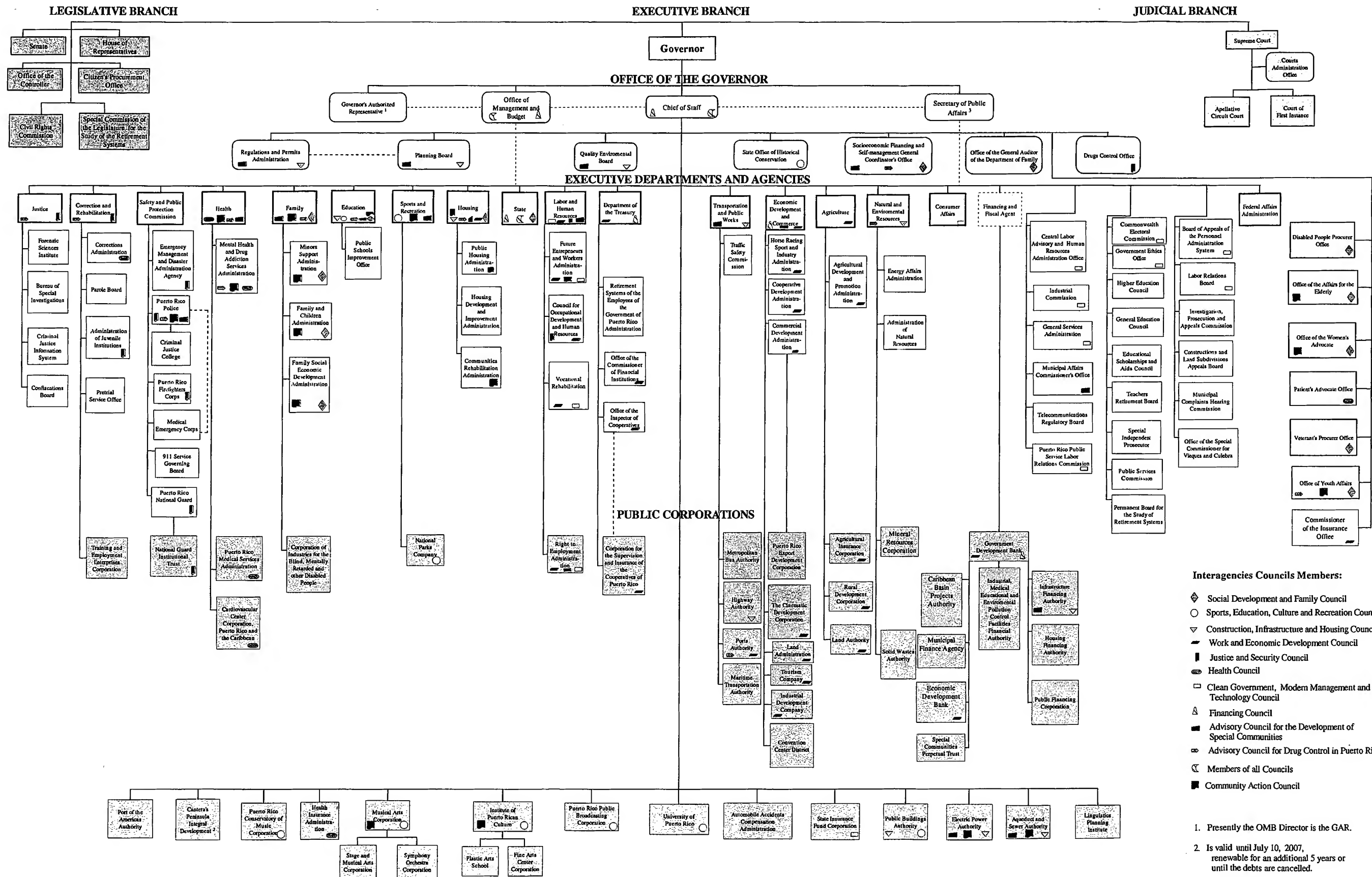
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## FISCAL OFFICERS

**Melba Acosta**  
Director, Office of Management  
and Budget

**Antonio Faria**  
President, Government  
Development Bank for  
Puerto Rico

# COMMONWEALTH OF PUERTO RICO



- Interagencies Councils Members:**
- ◆ Social Development and Family Council
  - Sports, Education, Culture and Recreation Council
  - ▽ Construction, Infrastructure and Housing Council
  - ▤ Work and Economic Development Council
  - ▥ Justice and Security Council
  - ▧ Health Council
  - ▨ Clean Government, Modern Management and Technology Council
  - ▩ Financing Council
  - Advisory Council for the Development of Special Communities
  - Advisory Council for Drug Control in Puerto Rico
  - ▬ Members of all Councils
  - ▮ Community Action Council

1. Presently the OMB Director is the GAR.
2. Is valid until July 10, 2007, renewable for an additional 5 years or until the debts are cancelled.
3. Include the Central Communications Office

# Certificate of Achievement for Excellence in Financial Reporting

Presented to

Commonwealth of  
Puerto Rico

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
June 30, 2002

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



A handwritten signature in cursive script, reading "Edward Haney".

President

A handwritten signature in cursive script, reading "Jeffrey R. Enen".

Executive Director

## **FINANCIAL SECTION**



**KPMG LLP**

American International Plaza  
Suite 1100  
250 Muñoz Rivera Avenue  
San Juan, PR 00918-1819

**Independent Auditors' Report**

The Honorable Governor and Legislature of the  
Commonwealth of Puerto Rico  
San Juan, Puerto Rico:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Puerto Rico (the Commonwealth) as of and for the year ended June 30, 2003, which collectively comprise the Commonwealth's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Commonwealth's management. Our responsibility is to express opinions on these financial statements based on our audit. We did not audit the financial statements of the Public Building Authority capital project fund (a major fund) which represents 1% and 0%, respectively, of the assets and revenue of the governmental activities. We also did not audit the financial statements of the following activities, funds, and component units:

- Public Housing Administration, the Office for the Improvements of Public Schools, Human Resources Occupational Development Council, and the Office for the Administration of the Assets of the Puerto Rico Urban Renewal and Housing Corporation which collectively represent 10% and 6%, respectively, of the assets and revenue of the general fund and 3% and 9%, respectively, of the assets and revenue of the governmental activities,
- The Additional Lottery System, which represents 85% and 39%, respectively, of the assets and revenue of the lotteries fund and 21% and 30%, respectively, of the assets and revenue of the business-type activities,
- Public Building Authority special revenue and debt service funds, which collectively represent 12% and 2%, respectively, of the assets and revenue of the aggregate remaining fund information and 2% and 0%, respectively, of the assets and revenue of the governmental activities,
- The pension trust funds, which represent 72% and 87%, respectively, of the assets and revenue of the aggregate remaining fund information, and
- Entities identified in note 2, that are presented as discretely presented component units, which collectively represent 65% and 85%, respectively, of the assets and revenue of the aggregate discretely presented component units.



These financial statements were audited by other auditors whose reports thereon have been furnished to us, and our opinions, insofar as they relate to the amounts included for the activities, funds, and component units indicated above, are based on the reports of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinions.

In our opinion, based on our audit and the reports of the other auditors, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Commonwealth of Puerto Rico, as of June 30, 2003, and the respective changes in financial position and cash flows, where applicable, thereof and the respective budgetary comparison for the general fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 3 through 18 and the schedule of funding progress on page 140 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Commonwealth's basic financial statements. The combining and individual fund financial statements and schedules listed in the table of contents are presented for purposes of additional analysis and are not a required part of the basic financial statements. These financial statements and combining schedules have been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, in our opinion, based on our audit and the report of the other auditors, are fairly stated in all material respects in relation to the basic financial statements taken as a whole. The introductory and statistical sections of this report listed in the table of contents have not been subjected to the auditing procedures applied by us and the other auditors in the audit of the basic financial statements and, accordingly, we express no opinion on them.

KPMG LLP

June 9, 2004

Stamp No. 1988256 of the Puerto Rico  
Society of Certified Public Accountants  
was affixed to the record copy of this report.

# **COMMONWEALTH OF PUERTO RICO**

## **Management's Discussion and Analysis**

June 30, 2003

Management of the Commonwealth of Puerto Rico (the Commonwealth) provides this Management's Discussion and Analysis for the readers of the Commonwealth's basic financial statements. This narrative overview and analysis of the financial activities of the Commonwealth is for the fiscal year ended June 30, 2003, and is intended to provide an easily readable explanation of the information provided in the attached basic financial statements. We encourage readers to consider this information with the Commonwealth's basic financial statements that follow.

### **FINANCIAL HIGHLIGHTS – PRIMARY GOVERNMENT**

#### **Government-wide Highlights**

- The Commonwealth reported a deficit of \$11 billion as of June 30, 2003, a deterioration in financial position of \$1.8 billion from last year's balances. The accumulated deficit is principally the result of the Commonwealth's practice of issuing debt and transferring such funds to its discretely presented component units in order for them to carry out the corresponding construction programs.
- The Commonwealth's total deficit increased by \$1.8 billion (a 19% increase) as a result of this year's operations. The governmental activities deficit increased by \$1.8 billion (a 17% increase), while net assets of the business-type activities showed a decrease of \$32.9 million (a 4% decrease).
- The Commonwealth's governmental activities had total revenue of \$12.2 billion which were exceeded by total expenses of \$14 billion, excluding transfers received from business-type activities amounting to \$279 million and a special item arising from the transfer of certain properties to municipalities amounting to \$204 million.

#### **Fund Highlights**

- As of June 30, 2003, the Commonwealth's governmental funds reported a combined ending fund balance of \$856 million, a decrease of \$200 million in comparison with the prior year.
- The general fund reported a deficit of \$80 million as of June 30, 2003.

#### **Long-Term Debt**

- Total long-term debt obligations as of June 30, 2003 was \$20 billion, from which \$2.8 billion are due within one year.
- The Commonwealth's total long-term debt obligations increased by \$2 billion (11%) during the current fiscal year.

### **OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as an introduction to the Commonwealth's basic financial statements. The Commonwealth's basic financial statements include three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. This report also

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

contains additional required supplementary information in addition to the basic financial statements themselves. These components are described below:

### **Basic Financial Statements**

The basic financial statements include two kinds of financial statements that present different views of the Commonwealth—the government-wide financial statements and the fund financial statements and combining major component units financial statements. These financial statements also include the notes to the basic financial statements that explain some of the information in the financial statements and provide more detail.

### ***Government-wide Financial Statements***

The government-wide financial statements provide a broad view of the Commonwealth's operations in a manner similar to a private sector business. The statements provide both short- and long-term information about the Commonwealth's financial position, which assists in assessing the Commonwealth's economic condition at the end of the fiscal year. These are prepared using the flow of economic resources measurement focus and the accrual basis of accounting. This basically means they follow methods that are similar to those used by most businesses. They take into account all revenue and expenses connected with the fiscal year even if cash involved has not been received or paid. The government-wide financial statements include two statements:

- ***Statement of Net Assets*** – This presents all of the government's assets and liabilities with the difference between the two reported as net assets (deficit). Over time, increases or decreases in the Commonwealth's net assets (deficit) may serve as a useful indicator of whether the financial position of the Commonwealth is improving or deteriorating.
- ***Statement of Activities*** – This presents information showing how the government's net assets changed during the most recent fiscal year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will not result in cash flows until future fiscal periods (such as uncollected taxes and earned but unused vacation leave). This statement also presents a comparison between direct expenses and program revenue for each function of the Commonwealth.

Both of the above financial statements have separate sections for three different types of Commonwealth programs or activities. These three types of activities are as follows:

- ***Governmental Activities*** – The activities in this section are mostly supported by taxes and intergovernmental revenue (federal grants). Most services normally associated with Commonwealth government fall into this category, including general government, public safety, health, public housing and welfare, education, and economic development.
- ***Business-Type Activities*** – These functions normally are intended to recover all or a significant portion of their costs through user fees and charges to external users of goods and services. These business-type



## COMMONWEALTH OF PUERTO RICO

### Management's Discussion and Analysis

June 30, 2003

activities of the Commonwealth include the operations of the following major funds: unemployment insurance trust fund (by the Commonwealth Employment Security Bureau) and the lotteries.

- **Component Units** – These are organizations that are legally separate from the Commonwealth, but the Commonwealth is either financially accountable for them, or the nature and significance of their relationship with the Commonwealth is such that their exclusion would cause the Commonwealth's financial statements to be misleading or incomplete. The Commonwealth has both blended and discretely presented component units.
  - **Blended Component Units** – Although legally separate entities, these are in substance part of the primary government's operations. Therefore, data from blended component units are integrated into the appropriate funds for reporting purposes.
  - **Discretely Presented Component Units** – These are operations for which the Commonwealth has financial accountability but they have certain independent qualities as well. For the most part, these entities operate similar to private sector businesses and the business-type activities described above. The Commonwealth's discretely presented component units are presented in two categories, major and nonmajor. This separation is determined by the relative size of the entities' assets, liabilities, revenue and expenses in relation to the total of all component units.

The Commonwealth's seven discretely presented major component units are:

- Government Development Bank for Puerto Rico
- Puerto Rico Highway and Transportation Authority
- Puerto Rico Electric Power Authority
- Puerto Rico Aqueduct and Sewer Authority
- Puerto Rico Infrastructure Financing Authority
- Puerto Rico Health Insurance Administration
- University of Puerto Rico

The Commonwealth's 35 nonmajor component units are combined into a single column for reporting in the fund financial statements. Complete financial statements of the individual component units can be obtained from their respective administrative offices. Addresses and other additional information about the Commonwealth's component units are presented in note 1 to the basic financial statements.

The government-wide financial statements can be found immediately following this discussion and analysis.

#### ***Fund Financial Statements***

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Commonwealth, like other states and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. The fund financial statements focus on individual parts of the Commonwealth government, reporting the Commonwealth's operations in more detail than the government-wide statements. All of the funds of the Commonwealth can be

## COMMONWEALTH OF PUERTO RICO

### Management's Discussion and Analysis

June 30, 2003

divided into three categories. It is important to note that these fund categories use different accounting approaches and should be interpreted differently. The three categories of funds are the following:

- ***Governmental Funds Financial Statements*** – Most of the basic services provided by the Commonwealth are financed through governmental funds. Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, the governmental fund financial statements focus on near-term inflows and outflows of expendable resources. They also focus on the balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating the government's near-term financing requirements. This approach is known as using the flow of current financial resources measurement focus and the modified accrual basis of accounting. These statements provide a detailed short-term view of the Commonwealth's finances that assists in determining whether there will be adequate financial resources available to meet the current needs of the Commonwealth. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenue, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and the governmental activities. These reconciliations are presented on the page immediately following each governmental fund financial statement.

The Commonwealth has four major governmental funds. That is, each major fund is presented in a separate column in the governmental fund balance sheet and in the governmental fund statement of revenue, expenditures, and changes in fund balances. The Commonwealth's four major governmental funds are the general fund, the debt service fund, the Public Buildings Authority capital projects fund, and The Children's Trust special revenue fund. The remaining nonmajor governmental funds are grouped and presented in a single column in the governmental fund financial statements. The basic governmental funds financial statements can be found immediately following the government-wide financial statements.

- ***Proprietary Funds Financial Statements*** – These funds are used to show activities that operate more like those of commercial enterprises. Because these funds charge fees for services provided to outside customers including local governments, they are known as enterprise funds. Proprietary funds provide the same type of information as the government-wide financial statements, only in more detail. Like the government-wide financial statements, proprietary fund financial statements use the accrual basis of accounting. There is no reconciliation needed between the government-wide financial statements for business-type activities and the proprietary fund financial statements. The Commonwealth has two major enterprise funds. As previously mentioned, they are the operations of the unemployment insurance trust fund (administered by the Commonwealth's Employment Security Bureau) and the lotteries. Other nonmajor proprietary funds are grouped and presented in a separate column in the enterprise fund financial statements. The basic proprietary funds financial statements can be found immediately following the governmental fund financial statements.

## COMMONWEALTH OF PUERTO RICO

### Management's Discussion and Analysis

June 30, 2003

- ***Fiduciary Funds and Similar Component Units Financial Statements*** – These funds are used to account for resources held for the benefit of parties outside the Commonwealth government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of these funds are not available to support the Commonwealth's own programs. The accounting used for fiduciary funds is much like that used for proprietary funds. They use the accrual basis of accounting. The Commonwealth's fiduciary funds are the pension trust funds (three separate retirement systems for employees, which are fiduciary component units of the Commonwealth), and the agency funds (which account for the assets held for distribution by the Commonwealth as an agent for other governmental units, other organizations, or individuals). The basic fiduciary funds and similar component units' financial statements can be found immediately following the proprietary fund financial statements.

#### ***Component Units Financial Statements***

As mentioned above, these are operations for which the Commonwealth has financial accountability but they have certain independent qualities as well, and they operate similar to private-sector businesses. The government-wide financial statements present information for the component units in a single column of the statement of net assets. Also, some information on the statement of changes in net assets is aggregated for component units. The combining statements of net assets and the combining statement of activities provide detail for each major component unit and the nonmajor component units in aggregate. The basic combining financial statements for major component units can be found immediately following the fiduciary funds financial statements.

#### ***Notes to the Financial Statements***

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and the fund financial statements. The notes to the financial statements can be found immediately following component units' financial statements.

#### **Required Supplementary Information**

The basic financial statements include within its notes a section of required supplementary information. This section includes information of funding progress for the Commonwealth's three separate retirement systems.

### **GOVERNMENT-WIDE FINANCIAL ANALYSIS**

#### **Net Assets**

As noted earlier, net assets may serve over time as a useful indicator of a government's financial position. Total assets and total liabilities of the Commonwealth's primary government at June 30, 2003 amounted to \$11.8 billion and \$23 billion, respectively, for a net deficit of \$11.2 billion, compared to \$9.4 billion net deficit at the beginning of the current year, as restated.

A portion of the Commonwealth's net assets (deficit) reflects its investment in capital assets such as land, buildings, and equipment, less any related debt used to acquire those assets that are still outstanding. The Commonwealth uses these capital assets to provide services to its residents; consequentially, these assets are not available for future spending. Although the Commonwealth's investment in its capital assets is reported net of

## COMMONWEALTH OF PUERTO RICO

### Management's Discussion and Analysis

June 30, 2003

related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

An additional portion of the Commonwealth's net assets (deficit) represents resources that are subject to external restrictions on how they may be used. An otherwise positive remaining balance would be used to meet the Commonwealth's ongoing obligations to citizens and creditors. Internally imposed designations of resources are not presented as restricted net assets. At the end of the current fiscal year, the Commonwealth is able to report positive balances in two categories of net assets, and a deficit, both for the government as a whole, as well as for its separate governmental and business-type activities.

As explained earlier, the net deficit of the primary government primarily results from the Commonwealth's practice of issuing debt and transferring such funds to the component units so that they can carry out the construction projects. The primary government retains the debt while the component units report the corresponding asset financed by such debt.

#### Commonwealth's Net Assets – Primary Government

June 30, 2003

(expressed in thousands)

	<b>Governmental activities</b>	<b>Business-type activities</b>	<b>Total</b>
Current assets	\$ 3,260,960	796,676	4,057,636
Capital assets	5,841,089	1,895	5,842,984
Other assets	1,432,203	431,650	1,863,853
<b>Total assets</b>	<b>10,534,252</b>	<b>1,230,221</b>	<b>11,764,473</b>
Current liabilities	5,411,156	274,402	5,685,558
Noncurrent liabilities	17,075,880	220,237	17,296,117
<b>Total liabilities</b>	<b>22,487,036</b>	<b>494,639</b>	<b>22,981,675</b>
Invested in capital assets, net of related debt	1,969,864	1,895	1,971,759
Restricted	19,749	736,947	756,696
Unrestricted	(13,942,397)	(3,260)	(13,945,657)
<b>Total net assets (deficit)</b>	<b>\$ (11,952,784)</b>	<b>735,582</b>	<b>(11,217,202)</b>

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Commonwealth's Net Assets – Primary Government

June 30, 2002

(expressed in thousands)

	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
Current assets	\$ 3,038,075	822,603	3,860,678
Capital assets	5,393,435	2,195	5,395,630
Other assets	1,493,736	429,092	1,922,828
Total assets	9,925,246	1,253,890	11,179,136
Current liabilities	4,835,998	229,708	5,065,706
Noncurrent liabilities	15,260,880	255,743	15,516,623
Total liabilities	20,096,878	485,451	20,582,329
Invested in capital assets, net of related debt	1,909,137	310	1,909,447
Restricted	4,616	769,804	774,420
Unrestricted	(12,085,385)	(1,675)	(12,087,060)
Total net assets (deficit)	\$ (10,171,632)	768,439	(9,403,193)

### Changes in Net Assets

The Commonwealth's net deficit increased by \$1.8 billion or 11% from last year's total net deficit. Approximately 57% of the Commonwealth's total revenue came from taxes, while 32% resulted from grants and contributions (primarily federal financial assistance). Charges for various goods and services provided 6% of the total revenue. The Commonwealth's expenses cover a range of services. The largest expenses were for education, public housing and welfare, and general government. In 2003, governmental activities' expenses exceeded program revenue, resulting in the use of \$9.3 billion in general revenue (mostly taxes). On the other hand, program revenue from business-type activities in 2003 exceeded expenses by approximately \$168 million.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Commonwealth of Puerto Rico's Changes in Net Assets – Primary Government Year ended June 30, 2003 (expressed in thousands)

	Governmental activities	Business-type activities	Total
Revenue:			
Program revenue:			
Charges for services	\$ 757,116	1,132,285	1,889,401
Operating grants and contributions	3,830,639	97,033	3,927,672
Capital grants and contributions	173,644	—	173,644
	<u>4,761,399</u>	<u>1,229,318</u>	<u>5,990,717</u>
General revenue:			
Income taxes	4,941,128	—	4,941,128
Property taxes	122,666	—	122,666
Excise taxes	1,894,729	—	1,894,729
Other taxes	3,055	—	3,055
Revenue from component units	111,752	1,038	112,790
Other	382,552	77,362	459,914
	<u>7,455,882</u>	<u>78,400</u>	<u>7,534,282</u>
Total revenue	<u>12,217,281</u>	<u>1,307,718</u>	<u>13,524,999</u>
Expenses:			
General government	2,324,715	—	2,324,715
Public safety	1,606,272	—	1,606,272
Health	1,903,811	—	1,903,811
Public housing and welfare	3,239,366	—	3,239,366
Education	3,375,815	—	3,375,815
Economic development	451,945	—	451,945
Intergovernmental	466,762	—	466,762
Interest and other	671,228	22,385	693,613
Lotteries	—	695,888	695,888
Unemployment	—	343,243	343,243
Total expenses	<u>14,039,914</u>	<u>1,061,516</u>	<u>15,101,430</u>
(Decrease) increase in net assets before transfers and special item	(1,822,633)	246,202	(1,576,431)
Transfers	279,060	(279,060)	—
Special item – land and recreational facilities transferred to municipalities	(203,514)	—	(203,514)
Decrease in net assets	(1,747,087)	(32,858)	(1,779,945)
Net assets (deficit), beginning of year (as previously reported)	(10,171,632)	768,440	(9,403,192)
Restatements to beginning net assets (deficit)	(34,065)	—	(34,065)
Net assets (deficit), end of year	<u>\$ (11,952,784)</u>	<u>735,582</u>	<u>(11,217,202)</u>

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Commonwealth of Puerto Rico's Changes in Net Assets – Primary Government Year ended June 30, 2002 (expressed in thousands)

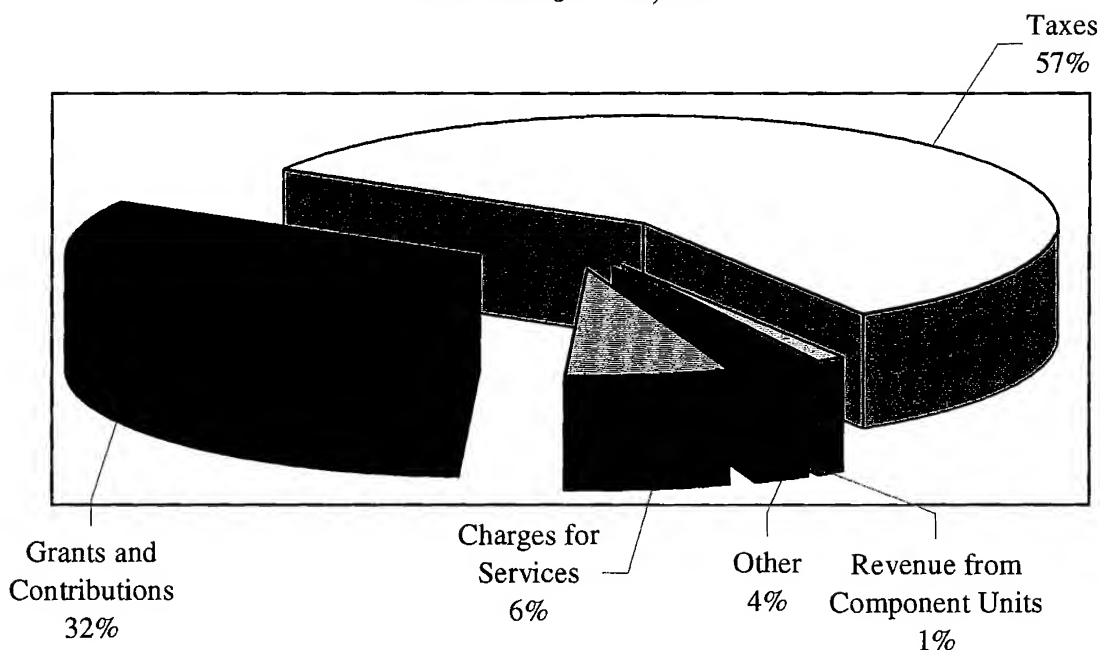
	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
Revenue:			
Program revenue:			
Charges for services	\$ 535,423	1,021,070	1,556,493
Operating grants and contributions	3,400,729	26,509	3,427,238
Capital grants and contributions	187,512	—	187,512
	<u>4,123,664</u>	<u>1,047,579</u>	<u>5,171,243</u>
General revenue:			
Income taxes	4,446,570	—	4,446,570
Property taxes	102,554	—	102,554
Excise taxes	1,713,098	—	1,713,098
Other taxes	1,963	—	1,963
Revenue from component units	228,118	3,370	231,488
Other	775,852	80,775	856,627
	<u>7,268,155</u>	<u>84,145</u>	<u>7,352,300</u>
Total revenue	<u>11,391,819</u>	<u>1,131,724</u>	<u>12,523,543</u>
Expenses:			
General government	1,429,265	—	1,429,265
Public safety	1,883,061	—	1,883,061
Health	1,990,852	—	1,990,852
Public housing and welfare	2,803,742	—	2,803,742
Education	3,477,373	—	3,477,373
Economic development	632,083	—	632,083
Intergovernmental	467,957	—	467,957
Interest and other	646,120	16,902	663,022
Lotteries	—	603,768	603,768
Unemployment	—	331,754	331,754
Total expenses	<u>13,330,453</u>	<u>952,424</u>	<u>14,282,877</u>
(Decrease) increase in net assets before transfers	(1,938,634)	179,300	(1,729,511)
Transfers	187,183	(187,183)	—
Special item – Puerto Rico Housing Bank and Finance Agency residual capital liquidation	123,785	—	123,785
Decrease in net assets	(1,627,666)	(7,883)	(1,635,549)
Net assets (deficit), beginning of year	<u>(8,543,966)</u>	<u>776,322</u>	<u>(7,767,644)</u>
Net assets (deficit), end of year	<u>\$ (10,171,632)</u>	<u>768,439</u>	<u>(9,403,193)</u>

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Revenue – Governmental Activities Year ended June 30, 2003



### Expenses – Governmental Activities Year ended June 30, 2003 (expressed in thousands)

Functions	Expenses
<b>Primary government:</b>	
<b>Governmental activities:</b>	
General government	\$ 2,324,715
Public safety	1,606,272
Health	1,903,811
Public housing and welfare	3,239,366
Education	3,375,815
Economic development	451,945
Intergovernmental	466,762
Interest and other	671,228
<b>Total governmental activities</b>	<b>\$ 14,039,914</b>



# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Governmental Activities

Governmental activities increased the Commonwealth's net deficit to \$12 billion. The decrease in net assets by the business-type activities is explained below. A comparison of the cost of services by function for the Commonwealth's governmental activities is shown below, along with the revenue used to cover the net expenses of the governmental activities (expressed in thousands).

#### Governmental Activities – Expenses Net of Program Revenue Year ended June 30, 2003 (expressed in thousands)

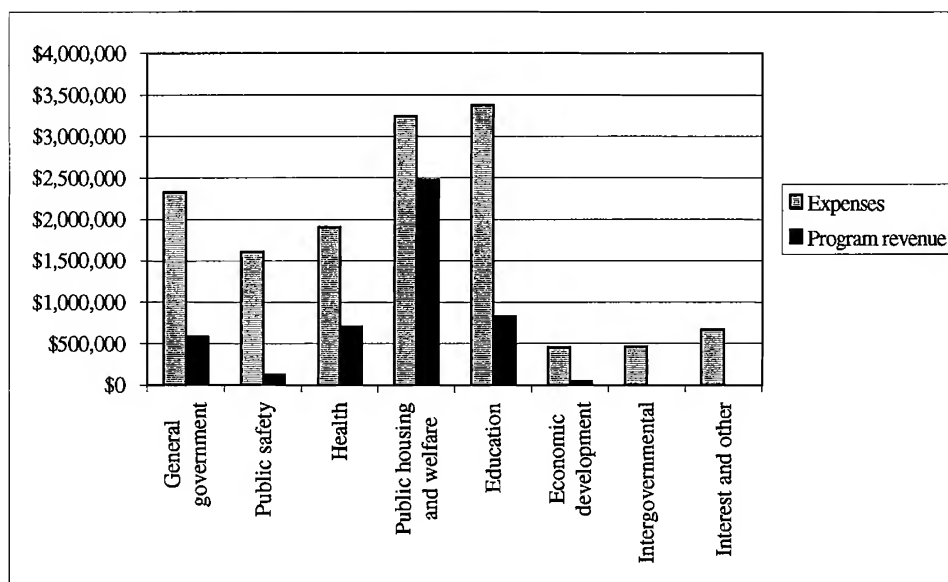
Expenses:	
General government	\$ (1,739,556)
Public safety	(1,481,715)
Health	(1,199,437)
Public housing and welfare	(766,335)
Education	(2,547,028)
Economic development	(406,454)
Intergovernmental	(466,762)
Interest and other	(671,228)
Total governmental activities net expenses	(9,278,515)
General revenue:	
Taxes	6,961,578
Revenue from component units	111,752
Special item – land and recreational facilities transferred to the municipalities	(203,514)
Transfers	279,060
Other	382,552
Increase in governmental activities net deficit	\$ <u>(1,747,087)</u>

## COMMONWEALTH OF PUERTO RICO

### Management's Discussion and Analysis

June 30, 2003

#### Expenses and Program Revenue – Governmental Activities Year ended June 30, 2003 (expressed in thousands)



#### Business-Type Activities

The business-type activities decreased the Commonwealth's net assets by \$32.9 million. This resulted predominantly from a \$21.8 million increase in net assets by the Commonwealth's revolving funds (nonmajor funds) offset by a \$54.7 million decrease in the net assets of the unemployment insurance trust fund. The Commonwealth's revolving funds represent loan funds which receive operating and capitalization grants from the U.S. Environmental Protection Agency and generate interest income through its lending activities. The net assets presented in this fund primarily represent the accumulation of interest earnings since the fund's inception.

#### FINANCIAL ANALYSIS OF THE COMMONWEALTH'S INDIVIDUAL FUNDS

As noted earlier, the Commonwealth uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

## **COMMONWEALTH OF PUERTO RICO**

### **Management's Discussion and Analysis**

June 30, 2003

#### **Governmental Funds**

The focus of the Commonwealth's governmental funds is to provide information on near-term inflows, outflows, and balances of expendable resources. Such information is useful in assessing the Commonwealth's financing requirements. In particular, unreserved fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year. As of the end of fiscal year 2003, the Commonwealth's governmental funds reported combined ending fund balance of \$856 million, a decrease of \$200 million or 19% in comparison with the prior year. There is \$428 million of fund balance reserved to indicate that it is not available for new spending because it has already been committed (1) to liquidate contracts and purchase orders of the prior fiscal year, (2) to pay debt service, or (3) for a variety of other restricted purposes.

The general fund is the chief operating fund of the Commonwealth. At the end of the current fiscal year, unreserved fund deficit of the general fund was \$436 million, while the total fund balance has a total deficit of \$80.2 million. The fund balance of the Commonwealth's general fund decreased by \$253.6 million as a result of the current fiscal year change in financial position. This is a 77% decrease when compared to the decrease reported in fiscal year 2002. Also, see additional related comments in the following section titled General Fund Budgetary Highlights.

#### **Proprietary Funds**

The Commonwealth's proprietary funds provide the same type of information found in the government-wide financial statements, but in more detail. As discussed in the business-type activities above, the Commonwealth's net assets decreased by \$32.9 million as a result of operations in the proprietary funds. This resulted from a \$55 million decrease (12% from prior year) in net assets by the unemployment insurance trust fund and an increase of net assets of \$22 million (7% from prior year) by the Commonwealth's other nonmajor enterprise funds.

#### **GENERAL FUND BUDGETARY HIGHLIGHTS**

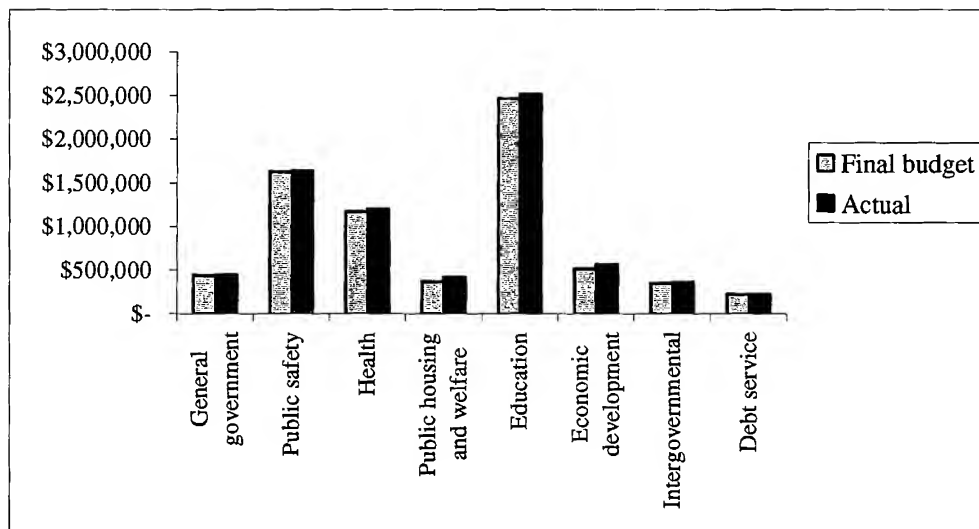
The original budget and the final amended budget remained substantially the same except for reclassifications of expenditures made throughout the year. Variances noted between actual expenditures and final amended budget primarily arise from expenditures financed through lines of credit arrangements. The fiscal year 2003 general fund actual expenditures, including debt service and transfers to other funds, were \$8 billion, \$14 million greater than the final budget. Such additional appropriations were made incrementally during the year.

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

June 30, 2003

### Expenditures – General Fund Budget vs. Actual Year ended June 30, 2003 (expressed in thousands)



As of June 30, 2003, there was an excess of expenditures and other uses over revenue and other sources of \$14 million.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

The Commonwealth's investment in capital assets for its governmental and business-type activities as of June 30, 2003, amounts to \$7.8 billion, net of accumulated depreciation of \$2 billion, leaving a book value of \$5.8 billion. This investment in capital assets includes land, buildings, building improvements, equipment, and construction in progress.

The net book value of capital assets at June 30, 2003 is distributed by function/activity in the following proportions: general government, 22%; public safety, 31%; health, 2%; public housing and welfare, 38%; and education, 7%. Actual expenditures to purchase or construct capital assets were approximately \$1.2 billion for the year. Depreciation charges for the year totaled \$270 million.

The infrastructure assets representing items that are normally immovable and of value only to the Commonwealth as roads, highways, bridges, toll facilities, water and sewer systems, lighting production, transmission and distribution systems, and similar items are principally owned by the component units of the

# COMMONWEALTH OF PUERTO RICO

## Management's Discussion and Analysis

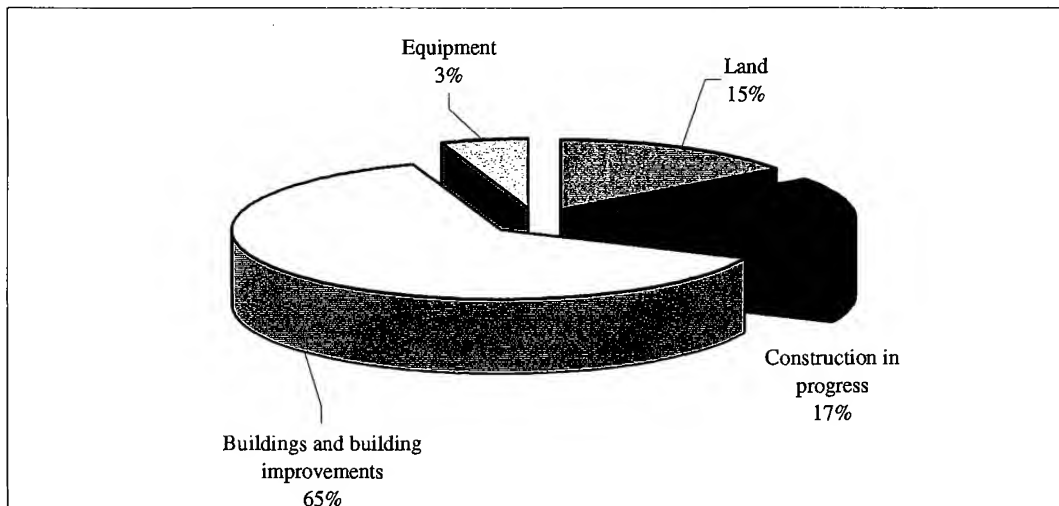
June 30, 2003

Commonwealth. Therefore, the infrastructure assets are reported within depreciable capital assets under the discretely presented component units' column. Additional information on the Commonwealth's capital assets can be found in note 12 to the basic financial statements that accompany this report.

### Commonwealth's Capital Assets – Primary Government June 30, 2003

(expressed in thousands)

	Governmental activities	Business-type activities	Total
Land	\$ 894,320	–	894,320
Construction in progress	964,608	–	964,608
Buildings and building improvements	3,825,250	–	3,825,250
Equipment	156,911	1,895	158,806
Total capital assets	\$ 5,841,089	1,895	5,842,984



### Debt Administration

General obligation bonds are backed by the full faith and credit of the Commonwealth, including the Commonwealth's power to levy additional taxes to ensure repayment of the debt.

The Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth, are not to be issued if the amount of the principal of, and interest on, such bonds and notes and on all such bonds and notes issued thereafter which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenue raised under the provisions of Commonwealth legislation and conveyed into the Treasury in the two fiscal years preceding the then current fiscal year. Section 2, Article VI of the Constitution does not limit the

## **COMMONWEALTH OF PUERTO RICO**

### **Management's Discussion and Analysis**

June 30, 2003

amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded. At June 30, 2003, the Commonwealth is in compliance with the debt limitation requirement.

Moody's and Standard & Poor's have given the Commonwealth's bonds ratings of "Baa1" and "A-", respectively. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained only from the respective rating agency.

The Commonwealth's total long-term obligations increased by \$2 billion during the current fiscal year, representing an 11% increase. Additional information on the Commonwealth's long-term debt obligations can be found in note 14 to the basic financial statements of this report.

### **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS AND RATES**

The unemployment rate for the Commonwealth of Puerto Rico is currently 12.5%, which is an increase from a rate of 10.5% a year ago.

Based on the projections of the Commonwealth's Planning Board, the Puerto Rico economy is expected to reflect a real growth of 2.7% for the fiscal year 2003. In nominal terms, the projection of the Planning Board anticipates an increase of 6.8% for the next fiscal year.

The consolidated budget for the fiscal year 2003-04 amounts to \$21.8 billion. From this amount, \$15.9 billion is assigned to operating expenses, \$3.3 billion to a permanent capital improvements program, and \$2.7 billion for the debt service.

### **REQUESTS FOR INFORMATION**

This financial report is designed to provide a general overview of the Commonwealth's finances for all of the Commonwealth's residents, taxpayers, customers, and investors and creditors. This financial report seeks to demonstrate the Commonwealth's accountability for the money it receives. Questions concerning any of the information provided in this report or requests for additional information should be addressed to: Department of the Treasury of the Commonwealth of Puerto Rico, Área de Contabilidad Central, P.O. Box 9024140, San Juan, Puerto Rico 00902-4140.

**COMMONWEALTH OF PUERTO RICO**

Statement of Net Assets

June 30, 2003  
(In thousands)

	<b>Primary government</b>			
	<b>Governmental activities</b>	<b>Business-type activities</b>	<b>Totals primary government</b>	<b>Component units</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 78,644	494,645	573,289	1,905,989
Cash and cash equivalents in governmental banks	801,409	259,493	1,060,902	333,599
Investments	553,596	36,024	589,620	5,400,051
Receivables, net of allowance for uncollectibles:				
Taxes	1,184,254	—	1,184,254	—
Unemployment insurance premiums	—	62,884	62,884	—
Intergovernmental	296,182	—	296,182	26,321
Accounts	141,074	—	141,074	635,507
Loans	14,546	—	14,546	1,878,717
Accrued interest	3,395	1,824	5,219	134,284
Other	57,312	14,088	71,400	70,819
Due from:				
Primary government	—	—	—	69,576
Component units	36,834	9,042	45,876	954,278
Other governmental entities	3,257	—	3,257	246,759
Internal balances	45,300	(45,300)	—	—
Inventories	39,656	—	39,656	223,640
Prepaid expenses	5,501	—	5,501	56,929
Restricted assets:				
Cash and cash equivalents	212,715	—	212,715	513,023
Cash and cash equivalents in governmental banks	1,031,161	—	1,031,161	205,414
Other restricted assets and investments	—	223,709	223,709	6,426,782
Long-term investments	—	—	—	232,201
Long-term receivables from:				
Intergovernmental	—	1,940	1,940	—
Loans	—	—	—	141,555
Long-term amounts due from:				
Primary government	—	—	—	72,937
Component units	—	129,386	129,386	24,306
Real estate held for sale or future development	72,948	—	72,948	274,719
Deferred expenses and other assets	115,379	40,591	155,970	406,473
Capital assets (net of accumulated depreciation):				
Land and other nondepreciable assets	1,858,928	—	1,858,928	11,093,403
Depreciable assets	3,982,161	1,895	3,984,056	14,265,568
<b>Total assets</b>	\$ 10,534,252	1,230,221	11,764,473	45,592,850

**COMMONWEALTH OF PUERTO RICO**

Statement of Net Assets, continued

June 30, 2003  
(In thousands)

	<b>Primary Government</b>			
	<b>Governmental activities</b>	<b>Business-type activities</b>	<b>Totals primary government</b>	<b>Component units</b>
<b>Liabilities</b>				
Accounts payable and accrued liabilities	\$ 1,185,725	12,257	1,197,982	1,915,252
Deposits and escrow liabilities	—	—	—	4,661,924
Tax refunds payable	203,589	—	203,589	—
Due to:				
Primary government	—	—	—	20,279
Component units	79,694	—	79,694	887,714
Other governmental entities	328	—	328	78,070
Securities lending transactions and reverse repurchase agreements	—	—	—	400,098
Interest payable	274,953	—	274,953	364,142
Deferred revenue	89,010	21,092	110,102	112,721
Other current liabilities	209,457	—	209,457	—
Tax revenue anticipation notes	800,000	—	800,000	—
Liability for automobile accident insurance and workmen compensation claims	—	—	—	978,914
Liabilities payable within one year:				
Commonwealth appropriation bonds	58,564	—	58,564	10,145
Bonds	147,660	—	147,660	537,166
Notes	1,239,557	774	1,240,331	918,996
Capital leases	11,081	—	11,081	—
Compensated absences	847,370	2,388	849,758	186,597
Lottery prizes	—	57,471	57,471	—
Unemployment insurance payable	—	180,069	180,069	—
Other long-term liabilities	218,434	351	218,785	80,188
Due to primary government – long-term portion	—	—	—	154,983
Due to component units – long-term portion	—	—	—	140,682
Deferred revenue – long-term portion	45,734	—	45,734	34,485
Liabilities payable after one year:				
Commonwealth appropriation bonds	2,738,867	—	2,738,867	982,706
Bonds	9,507,692	—	9,507,692	15,975,154
Notes	565,985	1,611	567,596	296,529
Capital leases	151,890	—	151,890	—
Net pension obligation	3,801,813	—	3,801,813	—
Compensated absences	303,071	1,321	304,392	269,516
Lottery prizes	—	217,305	217,305	—
Other long-term liabilities	6,562	—	6,562	404,782
<b>Total liabilities</b>	<b>22,487,036</b>	<b>494,639</b>	<b>22,981,675</b>	<b>29,411,043</b>
<b>Net assets</b>				
Invested in capital assets, net of related debt	1,969,864	1,895	1,971,759	12,025,393
Restricted for:				
Trust – nonexpendable	—	—	—	1,444,660
Capital projects	—	182,646	182,646	90,477
Debt service	—	—	—	945,654
Payment of unemployment and other insurance benefits	—	554,301	554,301	—
Affordable housing and related loan insurance programs	19,749	—	19,749	376,355
Student loans and other educational purposes	—	—	—	89,185
Other	—	—	—	332,762
Unrestricted deficit	(13,942,397)	(3,260)	(13,945,657)	877,321
<b>Total net assets (deficit)</b>	<b>\$ (11,952,784)</b>	<b>735,582</b>	<b>(11,217,202)</b>	<b>16,181,807</b>

See accompanying notes to basic financial statements.



COMMONWEALTH OF PUERTO RICO

Statement of Activities

Year ended June 30, 2003  
(In thousands)

Functions	Expenses	Program revenue		Net (expense) revenue and changes in net assets		
		Charges for services	Operating grants and contributions	Capital grants and contributions	Primary government	
					Governmental activities	Business-type activities
<b>Primary government:</b>						
<b>Governmental activities:</b>						
General government	\$ 2,324,715	499,528	85,631	—	(1,739,556)	(1,739,556)
Public safety	1,606,272	49,721	74,063	773	(1,481,715)	(1,481,715)
Health	1,903,811	159,444	544,930	—	(1,199,437)	(1,199,437)
Public housing and welfare	3,239,366	4,266	2,307,104	161,661	(766,335)	(766,335)
Education	3,375,815	3,344	814,233	11,210	(2,547,028)	(2,547,028)
Economic development	451,945	40,813	4,678	—	(406,454)	(406,454)
Intergovernmental	466,762	—	—	—	(466,762)	(466,762)
Interest and other	671,228	—	—	—	(671,228)	(671,228)
<b>Total governmental activities</b>	<b>14,039,914</b>	<b>757,116</b>	<b>3,830,639</b>	<b>173,644</b>	<b>(9,278,515)</b>	<b>(9,278,515)</b>
<b>Business-type activities:</b>						
Lotteries	695,888	871,731	—	—	—	175,843
Unemployment insurance	343,243	235,723	—	—	(107,520)	(107,520)
Other	22,385	24,831	97,033	—	—	99,479
<b>Total business-type activities</b>	<b>1,061,516</b>	<b>1,132,285</b>	<b>97,033</b>	<b>—</b>	<b>167,802</b>	<b>167,802</b>
<b>Total primary government</b>	<b>\$ 15,101,430</b>	<b>1,889,401</b>	<b>3,927,672</b>	<b>173,644</b>	<b>(9,278,515)</b>	<b>(9,110,713)</b>
<b>Component units:</b>						
Government Development Bank for Puerto Rico	494,962	467,307	144,122	37,027	—	—
Puerto Rico Highway and Transportation Authority	688,218	176,188	—	152,650	—	153,494
Puerto Rico Electric Power Authority	2,535,129	2,513,963	—	42,975	—	(359,380)
Puerto Rico Aqueduct and Sewer Authority	671,571	309,959	18,643	—	—	21,809
Puerto Rico Infrastructure Financing Authority	126,079	—	—	—	—	(342,969)
Puerto Rico Health Insurance Administration	1,319,577	348,950	—	—	—	(126,079)
University of Puerto Rico	1,093,706	157,603	236,852	7,296	—	(970,627)
Other component units	1,999,921	1,421,857	16,965	33,008	—	(691,955)
<b>Total component units</b>	<b>8,929,163</b>	<b>5,395,827</b>	<b>416,582</b>	<b>272,956</b>	<b>—</b>	<b>(528,091)</b>
						<b>(2,843,798)</b>
<b>Taxes:</b>						
Income taxes					4,941,128	4,941,128
Property taxes					122,666	122,666
Excise taxes					1,894,729	1,894,729
Other taxes					3,055	3,055
Revenue from global settlement agreement					101,849	101,849
Revenue from Tourism Company of Puerto Rico					72,612	72,612
Revenue from Government Development Bank for Puerto Rico					11,600	11,600
Revenue from Puerto Rico Infrastructure Financing Authority					—	—
Revenue from State Insurance Fund Corporation					27,540	1,038
Grants and contributions not restricted to specific programs					103,423	—
Payments from primary government					—	—
Unrestricted investment earnings					85,565	77,362
Other					91,715	91,715
Special item-transfer of properties to municipalities					(203,514)	—
Transfers					279,060	(279,060)
<b>Total general revenue, transfers, and special item</b>					<b>7,531,428</b>	<b>7,330,768</b>
<b>Change in net assets (deficit)</b>					<b>(1,747,087)</b>	<b>(32,858)</b>
<b>Net assets (deficit), beginning of year (as restated)</b>					<b>(10,205,697)</b>	<b>768,440</b>
<b>Net assets (deficit), end of year</b>					<b>(11,952,784)</b>	<b>(11,217,202)</b>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Balance Sheet – Governmental Funds

June 30, 2003  
(In thousands)

Assets	General	The Children's Trust special revenue	Debt service	PBA capital projects	Other governmental funds	Totals governmental funds
Cash and cash equivalents	\$ 55,416	—	—	—	23,228	78,644
Cash and cash equivalents in governmental banks	179,458	49,838	181,497	—	390,616	801,409
Investments	2,792	429,655	—	—	121,149	553,596
Receivables, net of allowance for uncollectibles:						
Taxes	1,153,789	—	30,465	—	—	1,184,254
Intergovernmental	296,182	—	—	—	—	296,182
Accounts	125,557	—	—	—	15,517	141,074
Loans	14,510	—	—	—	36	14,546
Accrued interest	1,850	779	766	—	—	3,395
Other	57,312	—	—	—	—	57,312
Due from:						
Other funds	45,300	—	—	18,242	83,034	146,576
Component units	11,237	—	—	—	25,597	36,834
Other governmental entities	3,257	—	—	—	—	3,257
Restricted assets:						
Cash, cash equivalents, and investments	151,298	—	—	54,638	6,779	212,715
Cash and cash equivalents in governmental banks	913,666	—	19,224	3,305	94,966	1,031,161
Real estate held for sale or disposition	65,415	—	—	—	—	65,415
Total assets	\$ 3,077,039	480,272	231,952	76,185	760,922	4,626,370

**COMMONWEALTH OF PUERTO RICO**

Balance Sheet – Governmental Funds, continued

June 30, 2003  
(In thousands)

<b>Liabilities and Fund Balances</b>	<b>General</b>	<b>The Children's Trust special revenue</b>	<b>Debt service</b>	<b>PBA capital projects</b>	<b>Other governmental funds</b>	<b>Totals governmental funds</b>
<b>Liabilities:</b>						
Accounts payable and accrued liabilities	\$ 1,001,183	8,924	—	121,618	52,524	1,184,249
Tax refunds payable	203,589	—	—	—	—	203,589
Due to:						
Other funds	89,111	—	—	12,165	—	101,276
Other governmental entities	328	—	—	—	—	328
Component units	59,643	—	—	—	—	59,643
Notes payable	—	—	—	85,245	—	85,245
Bonds payable	—	—	70,750	—	42,315	113,065
Interest payable	17,188	—	134,522	—	48,402	200,112
Deferred revenue	788,710	—	—	—	—	788,710
Tax revenue anticipation notes	800,000	—	—	—	—	800,000
Other liabilities	197,470	—	20,000	—	16,424	233,894
<b>Total liabilities</b>	<b>3,157,222</b>	<b>8,924</b>	<b>225,272</b>	<b>219,028</b>	<b>159,665</b>	<b>3,770,111</b>
<b>Fund balances:</b>						
Reserved for:						
Encumbrances	134,748	—	—	—	33,047	167,795
Debt service	2,792	—	—	—	—	2,792
Capital projects	14,245	—	—	—	—	14,245
Assets in liquidation	78,796	—	—	—	—	78,796
Low income housing assistance	32,177	—	—	—	—	32,177
Unreserved (deficit), reported in:						
General fund	(342,941)	—	—	—	—	(342,941)
Debt service funds	—	—	6,680	—	162,248	168,928
Special revenue funds	—	471,348	—	—	34,904	506,252
Capital project funds	—	—	—	(142,843)	371,058	228,215
<b>Total fund balances (deficit)</b>	<b>(80,183)</b>	<b>471,348</b>	<b>6,680</b>	<b>(142,843)</b>	<b>601,257</b>	<b>856,259</b>
<b>Total liabilities and fund balances</b>	<b>\$ 3,077,039</b>	<b>480,272</b>	<b>231,952</b>	<b>76,185</b>	<b>760,922</b>	<b>4,626,370</b>

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Reconciliation of the Balance Sheet to the Statement of Net Assets Governmental Funds

June 30, 2003  
(In thousands)

Amounts reported for governmental activities in the statement of net assets  
are different because:

Total fund balances of governmental funds	\$ 856,259
Inventories and prepaid expenses that are not available to pay for current period expenditures, and therefore are not recognized in the funds	45,157
Capital assets used in governmental activities are not financial resources and therefore are not reported in the funds	5,848,622
The difference between the proceeds of Qualified Zone Academic Bonds (QZAB) issued and the amounts paid to escrow agent to "early-defease" such bonds is deferred in the statement of net assets and amortized over the life of the QZAB. Since such difference did not provide current financial resources, it is not reported in the funds	(45,734)
Deferred revenue in governmental funds that are recognized as revenue in the governmental activities	699,700
Debt issued by the Commonwealth have associated costs that are paid from current available resources in the funds. However, these costs are deferred on the statement of net assets	100,534
Net pension asset of the Puerto Rico Judiciary Retirement System recognized in governmental activities is not a financial resource and therefore is not reported in the funds	14,845
Liabilities, including Commonwealth appropriation bonds, bonds payable, notes payable, capital leases payable, long-term portion of compensated absences and other long-term liabilities are not due and payable in the current period and therefore are not reported in the funds	(19,377,275)
Liability to component unit not due and payable in the current period and therefore is not reported in the funds.	(20,051)
Interest liabilities are not due and payable in the current period and therefore are not reported in the funds	(74,841)
Deficit of governmental activities	\$ <u>(11,952,784)</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Statement of Revenue, Expenditures, and Changes in Fund Balances  
Governmental Funds

Year ended June 30, 2003  
(In thousands)

	<u>General</u>	<u>The Children's Trust special revenue</u>	<u>Debt service</u>	<u>PBA capital projects</u>	<u>Other governmental funds</u>	<u>Totals governmental funds</u>
Revenue:						
Taxes:						
Income taxes	\$ 4,874,795	—	—	—	—	4,874,795
Property taxes	9,662	—	113,004	—	—	122,666
Excise taxes	1,894,729	—	—	—	—	1,894,729
Other taxes	3,055	—	—	—	—	3,055
Charges for services	780,905	—	—	—	—	780,905
Revenue from global settlement agreement	—	—	—	—	101,849	101,849
Revenue from component units:						
Government Development Bank for Puerto Rico	11,600	—	—	—	—	11,600
Tourism Company of Puerto Rico	72,612	—	—	—	—	72,612
State Insurance Fund Corporation	27,540	—	—	—	—	27,540
Intergovernmental	4,107,706	—	—	—	—	4,107,706
Interest and investment earnings	62,680	16,105	2,307	—	4,473	85,565
Other	99,905	—	181	—	315	100,401
Total revenue	<u>11,945,189</u>	<u>16,105</u>	<u>115,492</u>	<u>—</u>	<u>106,637</u>	<u>12,183,423</u>
Expenditures:						
Current:						
General government	1,395,847	214	—	—	378,095	1,774,156
Public safety	1,424,846	—	—	—	—	1,424,846
Health	1,906,418	2,299	—	—	—	1,908,717
Public housing and welfare	2,666,811	286,378	—	—	—	2,953,189
Education	3,255,004	42,244	—	—	—	3,297,248
Economic development	428,621	—	—	—	—	428,621
Intergovernmental	407,940	—	—	—	57,759	465,699
Capital outlays	730,190	—	—	262,402	192,384	1,184,976
Debt service:						
Principal	173,700	—	70,750	—	85,896	330,346
Interest and other	192,365	—	291,386	—	142,845	626,596
Debt issuance costs	—	11,864	35,406	—	11,595	58,865
Payment to refunded bond escrow agent	—	—	32,460	—	440,828	473,288
Total expenditures	<u>12,581,742</u>	<u>342,999</u>	<u>430,002</u>	<u>262,402</u>	<u>1,309,402</u>	<u>14,926,547</u>
Excess of expenditures over revenue	<u>(636,553)</u>	<u>(326,894)</u>	<u>(314,510)</u>	<u>(262,402)</u>	<u>(1,202,765)</u>	<u>(2,743,124)</u>
Other financing sources (uses):						
Transfers in	473,307	61,388	331,935	—	797,648	1,664,278
Transfers out	(586,500)	(709,533)	—	—	(89,185)	(1,385,218)
Long-term debt issued	437,239	1,171,200	—	69,075	563,676	2,241,190
Discount on bonds issued	—	(36,204)	—	—	—	(36,204)
Capital leases	58,897	—	—	—	—	58,897
Refunding bonds issued	—	—	1,315,491	—	439,195	1,754,686
Payment to refunded bond escrow agent	—	—	(1,315,491)	—	(439,195)	(1,754,686)
Total other financing sources (uses)	<u>382,943</u>	<u>486,851</u>	<u>331,935</u>	<u>69,075</u>	<u>1,272,139</u>	<u>2,542,943</u>
Net change in fund balances (deficit)	<u>(253,610)</u>	<u>159,957</u>	<u>17,425</u>	<u>(193,327)</u>	<u>69,374</u>	<u>(200,181)</u>
Fund balances (deficit), beginning of year (as restated)	<u>173,427</u>	<u>311,391</u>	<u>(10,745)</u>	<u>50,484</u>	<u>531,883</u>	<u>1,056,440</u>
Fund balances (deficit), end of year	<u>\$ (80,183)</u>	<u>471,348</u>	<u>6,680</u>	<u>(142,843)</u>	<u>601,257</u>	<u>856,259</u>

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Reconciliation of the Statement of Revenue, Expenditures, and Changes in Fund Balances to the Statement of Activities – Governmental Funds

Year ended June 30, 2003  
(In thousands)

Amounts reported for governmental activities in the statement of activities  
are different because:

Net change in fund balances – total governmental funds	\$ (200,181)
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense. This is the amount by which capital outlays (\$1,184,976) exceeded depreciation (\$269,826) in the current period	915,150
In the statement of activities, only the losses on the sale of capital assets is reported, whereas in the governmental funds, the proceeds from the sale increase financial resources. Therefore, the change in the net assets differs from the change in fund balance by the cost of the asset sold	(274,372)
Revenue in the statement of activities that do not provide current financial resources are not reported as revenue in the governmental funds	2,639
Debt proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of debt principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets. This is the amount by which proceeds (\$4,018,569) exceeded repayments (\$2,558,320)	(1,460,249)
Advances from a component unit provided current financial resources to governmental funds, but increase the liability to component unit in the statement of net assets	(20,051)
Income tax revenue that are not currently available are deferred in the governmental funds, but are accruable as revenue in the statement of activities. This is the amount by which deferred revenue increased during the year	66,333
Governmental funds do not report transfers of long-term assets or liabilities because such transfers do not represent financial resources, however they are recorded in the statement of activities. This amount represents the transfer of property by the Commonwealth to certain municipalities (see note 21)	(203,514)
Generally, inventory and prepayments are recorded as expenditures in the governmental funds when purchased rather than capitalized as an asset. However, these assets are capitalized in the statement of net assets. This amount represents the increase in inventory for the year	2,209
Debt issuance costs are expenditures to governmental funds, but are deferred assets in the statement of net assets. This is the amount of debt issue costs for the year	58,865
Certain interest and other costs reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount equivalent to the increase in interest payable (\$14,238), combined with the amortization of debt issue costs (\$7,670), and the net accretion and amortization of debt issue discount and deferred losses (\$42,696)	(64,226)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore are not reported as expenditures in the governmental funds. This is the amount by which the net increases in net pension obligation (\$582,691), Christmas bonus liability (\$24,463), liability in federal cost disallowances (\$10,646), and other liabilities (\$82) exceeded the net decreases in accrued compensated absences (\$46,650) and liability for legal claims and judgments (\$1,542)	(569,690)
Change in deficit of governmental activities	\$ <u>(1,747,087)</u>

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Statement of Revenue and Expenditures – Budget and Actual – Budget Basis – General Fund

Year ended June 30, 2003  
(In thousands)

	<u>Original budget</u>	<u>Amended budget</u>	<u>Actual</u>	<u>Variance</u>
Revenue:				
Income taxes	\$ 5,155,000	5,155,000	4,909,725	(245,275)
Excise taxes	1,958,000	1,958,000	1,868,287	(89,713)
Other taxes	86,000	86,000	88,701	2,701
Charges for services	153,000	153,000	181,261	28,261
Intergovernmental	30,000	30,000	26,104	(3,896)
Revenue from component units	93,000	123,000	120,020	(2,980)
Other	79,000	49,000	147,059	98,059
Total revenue	<u>7,554,000</u>	<u>7,554,000</u>	<u>7,341,157</u>	<u>(212,843)</u>
Expenditures:				
Current:				
General government	481,482	435,327	442,825	(7,498)
Public safety	1,611,807	1,631,344	1,637,188	(5,844)
Health	1,185,546	1,170,696	1,199,891	(29,195)
Public housing and welfare	356,449	368,990	419,406	(50,416)
Education	2,472,107	2,465,212	2,516,072	(50,860)
Economic development	509,930	512,329	565,993	(53,664)
Intergovernmental	346,900	350,254	361,380	(11,126)
Debt service:				
Principal	69,740	69,740	69,740	—
Interest and other	153,333	153,333	153,333	—
Total expenditures	<u>7,187,294</u>	<u>7,157,225</u>	<u>7,365,828</u>	<u>(208,603)</u>
Excess (deficiency) of revenue over (under) expenditures	<u>366,706</u>	<u>396,775</u>	<u>(24,671)</u>	<u>(421,446)</u>
Other financing sources (uses):				
Transfers in	282,000	282,000	263,586	(18,414)
Transfers out	(648,706)	(678,775)	(677,214)	1,561
Notes payable issued	—	—	424,337	424,337
Total other financing sources (uses)	<u>(366,706)</u>	<u>(396,775)</u>	<u>10,709</u>	<u>407,484</u>
Excess of expenditures and other uses over revenue and other sources	<u>\$ —</u>	<u>—</u>	<u>(13,962)</u>	<u>(13,962)</u>

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Statement of Net Assets – Proprietary Funds

June 30, 2003

(In thousands)

	Business-type activities – enterprise funds			
	Unemployment Insurance Trust	Lotteries	Other funds	Totals
<b>Assets</b>				
Current assets:				
Cash and cash equivalents	\$ 482,707	11,938	—	494,645
Cash and cash equivalents in governmental banks	69,159	48,788	141,546	259,493
Accounts and loans receivable, net:				
Insurance premiums, net	58,307	—	4,577	62,884
Component units	—	—	9,042	9,042
Accrued interest	25	—	1,800	1,825
Other	8,332	5,357	398	14,087
Investments:				
Unrestricted, including collateral from securities lending transactions	—	—	36,024	36,024
Restricted	—	223,709	—	223,709
Total current assets	618,530	289,792	193,387	1,101,709
Noncurrent assets:				
Loans receivable, excluding current portion, net:				
Component units	—	—	129,386	129,386
Intergovernmental	—	—	1,940	1,940
Capital assets, net	—	1,895	—	1,895
Other	—	40,591	—	40,591
Total assets	618,530	332,278	324,713	1,275,521
<b>Liabilities and Net Assets</b>				
Current liabilities:				
Accounts payable and accrued liabilities	—	11,562	1,046	12,608
Due to other funds	16,698	28,602	—	45,300
Deferred revenue	7,357	13,705	30	21,092
Compensated absences	—	1,776	612	2,388
Lottery awards	—	57,471	—	57,471
Insurance benefits payable	178,954	—	1,115	180,069
Notes payable	—	1,003	—	1,003
Total current liabilities	203,009	114,119	2,803	319,931
Noncurrent liabilities:				
Compensated absences	—	837	484	1,321
Lottery awards	—	217,305	—	217,305
Due to component units	—	1,308	—	1,308
Notes payable	—	74	—	74
Total liabilities	203,009	333,643	3,287	539,939
Net assets:				
Invested in capital assets	—	1,895	—	1,895
Restricted for:				
Payment of insurance benefits	415,521	—	138,780	554,301
Capital projects	—	—	182,646	182,646
Unrestricted	—	(3,260)	—	(3,260)
Total net assets (deficit)	\$ 415,521	(1,365)	321,426	735,582

See accompanying notes to basic financial statements.



# COMMONWEALTH OF PUERTO RICO

## Statement of Revenue, Expenses, and Changes in Net Assets Proprietary Funds

Year ended June 30, 2003  
(In thousands)

	Business-type activities – enterprise funds			
	Unemployment Insurance Trust	Lotteries	Other funds	Totals
Operating revenue:				
Lottery ticket sales	\$ —	871,072	—	871,072
Insurance premiums	234,438	—	19,754	254,192
Interest	—	—	5,077	5,077
Other	1,285	659	—	1,944
Total operating revenue	235,723	871,731	24,831	1,132,285
Operating expenses:				
Lottery awards	—	529,766	—	529,766
Insurance benefits	343,243	—	5,529	348,772
General, administrative, and other operating expenses	—	165,757	16,856	182,613
Depreciation and amortization	—	365	—	365
Total operating expenses	343,243	695,888	22,385	1,061,516
Operating income (loss)	(107,520)	175,843	2,446	70,769
Nonoperating revenue (expenses):				
Contributions from federal government	81,955	—	15,078	97,033
Contributions from component unit	—	—	1,038	1,038
Interest and investment earnings	32,368	—	1,526	33,894
Gain on sale of investment	—	43,468	—	43,468
Total nonoperating revenue (expenses)	114,323	43,468	17,642	175,433
Income before transfers	6,803	219,311	20,088	246,202
Transfers from general fund	—	—	1,742	1,742
Transfers to general fund	(61,491)	(219,311)	—	(280,802)
Net change in net assets (deficit)	(54,688)	—	21,830	(32,858)
Net assets (deficit), beginning of year (as restated)	470,209	(1,365)	299,596	768,440
Net assets (deficit), end of year	\$ 415,521	(1,365)	321,426	735,582

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**

Statement of Cash Flows  
Proprietary Funds

Year ended June 30, 2003  
(In thousands)

	Business-type activities – enterprise funds			
	Unemployment insurance trust	Lotteries	Other funds	Totals
Cash flows from operating activities:				
Receipts from customers and users	\$ 234,789	871,131	19,603	1,125,523
Other receipts	1,974	642	—	2,616
Payments to suppliers and employees	—	(284,612)	(16,277)	(300,889)
Payment of lottery prizes	—	(476,391)	—	(476,391)
Payments of insurance benefits	(313,417)	—	(5,373)	(318,790)
Other payments	—	—	(834)	(834)
Net cash (used in) provided by operating activities	(76,654)	110,770	(2,881)	31,235
Cash flows from noncapital financing activities:				
Intergovernmental grants and contributions	81,955	—	14,957	96,912
Transfers from general fund	14,258	—	2,900	17,158
Proceeds from issuance of notes payable to component units	—	255	—	255
Transfers to general fund	(61,491)	(219,311)	—	(280,802)
Net cash provided by (used in) noncapital financing activities	34,722	(219,056)	17,857	(166,477)
Cash flows from capital and related financing activities:				
Capital expenditures	—	(66)	—	(66)
Principal payments of notes payable	—	(808)	—	(808)
Net cash used in capital and related financing activities	—	(874)	—	(874)
Cash flows from investing activities:				
Proceeds from sales and maturities of investments	—	326,503	—	326,503
Interest received on deposits and investments	32,392	—	7,040	39,432
Purchases of investments	—	(223,709)	—	(223,709)
Principal collected on loans	—	—	10,961	10,961
Loans originated	—	—	(17,160)	(17,160)
Net cash provided by investing activities	32,392	102,794	841	136,027
Net (decrease) increase in cash and cash equivalents	(9,540)	(6,366)	15,817	(89)
Cash and cash equivalents, beginning of year	561,406	67,092	125,729	754,227
Cash and cash equivalents, end of year	\$ 551,866	60,726	141,546	754,138
Reconciliation of operating income to net cash (used in) provided by operating activities:				
Operating (loss) income	\$ (107,520)	175,843	2,446	70,769
Adjustments to reconcile operating (loss) income to net cash (used in) provided by operating activities:				
Depreciation and amortization	—	365	—	365
(Decrease) increase in accounts and loans receivable	(194)	42	(8,701)	(8,853)
Interests earned on deposits loans and investments	—	—	3,472	3,472
Changes in operating assets and liabilities:				
Increase in other assets	—	(40,457)	—	(40,457)
Decrease in inventories	—	—	16	16
Decrease in obligation for unpaid lottery awards	—	(22,392)	—	(22,392)
Decrease in due to other funds	—	(3,592)	—	(3,592)
Increase (decrease) in deferred revenue	1,234	(4,545)	14	(3,297)
Increase (decrease) in compensated absences	—	(11)	52	41
Increase in liability for benefits	29,826	—	156	29,982
Increase (decrease) in accounts payable and accrued liabilities	—	5,517	(336)	5,181
Total adjustments	30,866	(65,073)	(5,327)	(39,534)
Net cash (used in) provided by operating activities	\$ (76,654)	110,770	(2,881)	31,235

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Statement of Fiduciary Net Assets

June 30, 2003

(In thousands)

	<b>Pension trust funds</b>	<b>Special deposits agency fund</b>
<b>Assets</b>		
Cash and cash equivalents:		
Unrestricted	\$ 120,316	506,200
Restricted	2,236	—
Cash and cash equivalents in governmental banks:		
Unrestricted	33,301	88,326
Restricted	653	—
Investments:		
Debt and equity securities, at fair value	3,088,009	13,095
Investment in PRTA Holdings, at appraised value	362,670	—
Other	34,735	—
Receivables, net:		
Accounts	44,976	—
Loans and advances	631,629	18,983
Accrued interest and dividends	14,104	—
Other	19,491	—
Other assets	42,957	482
<b>Total assets</b>	<b>4,395,077</b>	<b>627,086</b>
<b>Liabilities</b>		
Accounts payable and accrued liabilities	181,885	627,086
Securities lending transactions	38,404	—
Bonds payable	22,943	—
<b>Total liabilities</b>	<b>243,232</b>	<b>627,086</b>
<b>Net Assets</b>		
Net assets held in trust for pension and other benefits	\$ <u>4,151,845</u>	<u>—</u>

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Statement of Changes in Fiduciary Net Assets – Pension Trust Funds

Year ended June 30, 2003

(In thousands)

### Additions:

#### Contributions:

Sponsor	\$ 430,783
Participants	383,229
Special	45,421

Total contributions	<u>859,433</u>
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Interest	127,323
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Dividends	59,242
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Net change in fair value of investments, including realized losses on sale and maturities of investments	(76,253)
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Investment expenses	<u>(9,188)</u>
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Net interest and investment income	<u>101,124</u>
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Other income	<u>12,137</u>
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Total additions	<u>972,694</u>
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### Deductions:

Pension and other benefits	952,660
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Refunds of contributions	25,610
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General and administrative	49,785
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Total deductions	<u>1,028,055</u>
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Net change in net assets held in trust for pension and other benefits	(55,361)
--	----------

Net assets held in trust for pension and  
other benefits:

Beginning of year	<u>4,207,206</u>
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End of year	<u><u>\$ 4,151,845</u></u>
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See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Combining Statement of Net Assets – Major Component Units

June 30, 2003  
(In thousands)

		Assets									
		Government Development Bank for Puerto Rico	Puerto Rico Highway and Transportation Authority	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Infrastructure Financing Authority	Puerto Rico Health Insurance Administration	University of Puerto Rico	Nonmajor component units	Total component units	
Current assets:	Cash and cash equivalents	\$ 1,490,233	42,525	50,451	15,592	56,658	14,896	72,133	163,501	1,905,989	
	Cash and cash equivalents in governmental banks	—	—	—	109,018	86,581	1,728	30,166	106,106	333,599	
	Investments, including collateral from securities lending transactions	2,385,618	—	—	—	496,098	—	35,012	2,483,323	5,400,051	
	Receivables, net:										
	Intergovernmental	10,601	7,511	—	—	—	4,769	366	3,074	26,321	
	Accounts	—	3,841	386,039	26,123	—	—	8,564	210,940	635,507	
	Loans and advances	1,836,316	—	—	—	—	—	—	42,401	1,878,717	
	Accrued interest	92,210	2,194	1,253	—	19,882	7	—	18,738	134,284	
	Other governmental entities	—	—	103,629	35,873	—	—	45,447	61,810	246,759	
	Other	—	—	—	9,251	—	13,575	18,977	29,016	70,819	
	Due from:										
	Primary government	6,217	—	12,653	—	1,200	—	32,570	16,936	69,576	
	Component units	764,877	—	11,688	22,196	18,000	—	11,426	126,091	954,278	
	Inventories	—	—	184,309	—	—	—	6,922	32,409	223,640	
	Prepays	—	3,608	20,808	1,940	1,484	400	14,567	14,122	56,929	
	Total current assets	6,586,072	59,679	770,830	219,993	679,903	35,375	276,150	3,308,467	11,936,469	
Noncurrent assets:	Restricted assets:										
	Cash and cash equivalents	58,431	5,080	322,289	1,051	—	—	3,344	122,828	513,023	
	Cash and cash equivalents in governmental banks	—	43,781	—	28,638	—	—	121	132,874	205,414	
	Investments and other restricted assets	2,029,704	762,646	408,457	—	1,427,480	—	69,017	1,729,478	6,426,782	
	Investments	—	—	—	—	—	—	—	232,201	232,201	
	Receivables:										
	Loans, interest, and other	—	—	—	—	—	—	1,857	139,698	141,555	
	Due from:										
	Primary government	20,051	—	29,416	—	—	—	23,470	—	72,937	
	Component units	—	—	—	—	—	—	—	24,306	24,306	
	Property held for sale and future development	28,525	—	39,751	—	—	—	—	206,443	274,719	
	Capital assets not being depreciated	2,955	6,993,322	1,469,187	377,973	773,984	—	180,952	1,293,030	11,093,403	
	Capital assets, depreciable, net	11,862	5,324,029	3,094,346	4,092,031	294	5,630	389,625	1,347,751	14,265,568	
	Deferred expenses and other assets	129,373	109,553	75,103	20,652	20,884	—	—	50,908	406,473	
	Total noncurrent assets	2,280,901	13,240,411	5,438,549	4,520,345	2,222,642	5,630	668,386	5,279,517	33,656,381	
	Total assets	\$ 8,866,973	13,300,090	6,209,379	4,740,338	2,902,545	41,005	944,536	8,587,984	45,592,850	

**COMMONWEALTH OF PUERTO RICO**  
Combining Statement of Net Assets – Major Component Units, continued  
June 30, 2003  
(In thousands)

	Government Development Bank for Puerto Rico	Puerto Rico Highway and Transportation Authority	Puerto Rico Electric Power Authority	Puerto Rico Aqueduct and Sewer Authority	Puerto Rico Infrastructure Financing Authority	Puerto Rico Health Insurance Administration	University of Puerto Rico	Nonmajor component units	Total component units
<b>Liabilities</b>									
Current liabilities:									
Accounts payable and accrued liabilities	\$ 174,973	209,761	417,221	224,245	69,925	33,685	83,590	701,852	1,915,252
Deposits and escrow liabilities	3,779,541	—	141,863	6,576	—	—	—	733,944	4,661,924
Due to:									
Primary government	6,924	—	—	9,042	—	—	—	4,313	20,279
Component units	—	—	60,000	56,161	23,347	—	508	747,698	887,714
Other governmental entities	—	—	38,576	20,344	—	—	—	19,150	78,070
Securities lending transactions and reverse repurchase agreements	190,017	—	—	—	—	—	—	182,781	372,798
Interest payable	12,016	108,996	121,942	10,822	39,817	—	1,062	69,487	364,142
Deferred revenue	761,167	—	—	—	—	—	—	112,721	112,721
Notes payable, current portion	102	—	125,000	—	106	—	—	32,829	918,996
Commonwealth appropriation bonds	84,390	10,435	285,407	7,583	24,580	—	21,170	2,664	10,145
Bonds payable, current portion	4,857	—	69,753	22,858	105	322	17,556	103,601	537,166
Accrued compensated absences	—	—	—	—	—	—	—	71,146	186,597
Reserves for automobile accident benefit payments	—	23,084	—	—	—	—	—	978,914	978,914
Current portion of other long-term liabilities	—	—	19,452	—	—	12	3,175	34,465	80,188
Total current liabilities	5,013,987	352,276	1,279,214	364,904	157,880	34,019	127,061	3,795,565	11,124,906
Noncurrent liabilities									
Due to:									
Primary government	—	—	—	129,386	—	—	—	25,597	154,983
Component units	—	—	—	—	8,649	—	17,000	115,033	140,682
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—	—	—	27,300	27,300
Deferred revenue	—	—	29,160	—	—	—	—	5,325	34,485
Notes payable	9,927	—	5,000	—	—	—	—	291,529	296,529
Commonwealth appropriation bonds	1,687,280	5,303,959	4,221,311	704,857	10,225	—	411,115	257,697	982,706
Bonds payable	—	16,235	128,912	811,167	1,960,311	—	89,840	1,580,011	15,975,154
Accrued compensated absences	—	18,000	1,003	18,816	133	544	15,036	269,516	269,516
Other long-term liabilities	1,697,207	5,338,194	4,385,386	1,720,906	1,985,318	544	45,230	277,869	404,782
Total noncurrent liabilities	6,711,194	5,690,470	5,664,600	2,085,810	2,143,198	34,563	690,246	2,595,397	18,286,137
Total liabilities								6,390,962	29,411,043
Net assets:									
Invested in capital assets, net of related debt	14,817	7,070,203	175,301	2,762,535	214,553	5,615	150,640	1,631,729	12,025,393
Restricted for:									
Trust – nonexpendable	—	—	—	—	1,444,660	—	—	—	1,444,660
Capital projects	—	66,421	—	—	(15,807)	—	11,980	27,883	90,477
Debt service	56,920	437,667	366,809	—	14,941	—	38,744	945,654	376,355
Affordable housing and related loan insurance programs	376,355	—	—	—	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	—	—	81,321	7,864	89,185
Other specified purposes	—	—	—	28,579	13,551	—	—	290,632	332,762
Unrestricted	1,707,687	35,329	2,669	(136,586)	(912,551)	827	(28,395)	208,341	877,321
Total net assets	2,155,779	7,609,620	544,779	2,654,528	759,347	6,442	254,290	2,197,022	16,181,807
Total liabilities and net assets	\$ 8,866,973	\$ 13,300,090	\$ 6,209,379	\$ 4,740,338	\$ 2,902,545	\$ 41,005	\$ 944,536	\$ 8,587,984	\$ 45,592,850

See accompanying notes to basic financial statements.

**COMMONWEALTH OF PUERTO RICO**  
Combining Statement of Activities – Major Component Units  
Year ended June 30, 2003  
(In thousands)

Component units	General revenue and transfers												Net assets, beginning of year	Net assets, end of year	
	Expenses	Program revenue		Net revenue (expenses) and changes in net assets	Payments from primary government	Payments from (to) other component units	Grants and contributions not restricted to specific programs	Taxes	Interest and investment earnings	Gain in sale of assets	Other	Change in net assets			
		Charges for services	Operating grants and contributions												Capital grants and contributions
Government															
Development Bank for Puerto Rico	\$ 494,962	467,307	144,122	37,027	153,494	—	—	—	97	—	—	—	153,591	2,002,188	2,155,779
Puerto Rico Highway and Transportation Authority	688,218	176,188	—	152,650	(359,380)	—	—	—	308,804	23,203	—	—	(27,373)	7,636,993	7,609,620
Puerto Rico Electric Power Authority	2,535,129	2,513,963	—	42,975	21,809	—	—	—	—	20,296	—	10,329	52,434	492,345	544,779
Puerto Rico Aqueduct and Sewer Authority	671,571	309,959	18,643	—	(342,969)	443,847	41,981	—	—	—	—	42,972	185,831	2,468,697	2,654,528
Puerto Rico Infrastructure	126,079	—	—	—	(126,079)	74,732	(41,981)	—	—	275,217	—	—	181,889	577,458	759,347
Financing Authority															
Puerto Rico Health Insurance	1,319,577	348,950	—	—	(970,627)	963,439	—	—	—	681	—	—	(6,507)	12,949	6,442
Administration															
University of Puerto Rico	1,093,706	157,603	236,852	7,296	(691,955)	696,242	—	4,048	—	3,101	—	1,391	12,827	241,463	254,290
Nonmajor component units	1,999,921	1,421,857	16,965	33,008	(528,091)	482,425	—	3,406	49,739	263,676	10,507	7,903	289,565	1,907,457	2,197,022
Total component units	\$ 8,929,163	5,395,827	416,582	272,956	(2,843,798)	2,660,685	—	7,454	358,543	586,271	10,507	62,595	842,257	15,339,550	16,181,807

See accompanying notes to basic financial statements.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### (1) **Summary of Significant Accounting Policies**

The Commonwealth of Puerto Rico (the Commonwealth) was constituted on July 25, 1952, under the provisions of its Constitution as approved by the people of Puerto Rico and the U.S. Congress. The Commonwealth's Constitution provides for the separation of powers of the executive, legislative, and judicial branches of the government. The Commonwealth assumes responsibility for public safety, health, public housing and welfare, education, and economic development.

The accompanying basic financial statements of the Commonwealth have been prepared in conformity with accounting principles generally accepted (GAAP) in the United States of America as prescribed by the Governmental Accounting Standards Board (GASB).

The accompanying basic financial statements present the financial position of the Commonwealth and its various funds, the results of operations of the Commonwealth and its various funds and fund types, and the cash flows of the proprietary funds. The basic financial statements are presented as of June 30, 2003, and for the year then ended. The basic financial statements include the various departments, agencies, boards, commissions, public trusts, and public corporations and any other organizational units governed by the Puerto Rico Legislature and/or officers of the Commonwealth.

#### *(a) The Financial Reporting Entity*

The accompanying basic financial statements include all departments, agencies, and governmental entities whose funds are under the custody and control of the Secretary of the Treasury of the Commonwealth and the Commonwealth's component units pursuant to Act No. 230 of July 23, 1974, as amended, known as Commonwealth of Puerto Rico Accounting Law. The Commonwealth has considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth's financial statements to be misleading or incomplete. The GASB has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the Commonwealth to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on the Commonwealth.

As required by GAAP, these basic financial statements present the Commonwealth and its component units.

#### *(b) Component Units*

Component units are entities that are legally separate organizations for which the Commonwealth's elected officials are financially accountable or other organizations for which the nature and significance of their relationship with the Commonwealth are such that exclusion would cause the Commonwealth's basic financial statements to be misleading and incomplete. GAAP details two methods of presentation: blending the financial data of the component units' balances and transactions in a manner similar to the presentation of the Commonwealth's balances and



## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

transactions; or discrete presentation of the component units' financial data in columns separate from the Commonwealth's balances and transactions. The Commonwealth can impose its will on each of the component units through appointment of the members of their governing authorities. The financial statements of the component units discussed below have been included in the financial reporting entity either as blended component units or as discretely presented component units in accordance with GASB Statement No. 14, *The Financial Reporting Entity* (GASB No. 14), as amended.

#### **Blended Component Units**

The following entities, while legally separate from the Commonwealth, meet the criteria to be reported as part of the primary government because they provide services entirely or almost entirely to the Commonwealth.

***Public Buildings Authority (PBA)*** – PBA is governed by a seven-member board of which the Secretary of the Department of Transportation and Public Works (DTPW) of the Commonwealth is a permanent member and the other six members are appointed by the Governor of Puerto Rico with the advice and consent of the Senate. These members are appointed for a period of five years. It is a legally separate entity, whose activities are blended within the primary government because it exists to construct, purchase, or lease office, school, health, correctional, social welfare, and other facilities for lease to the Commonwealth's departments, component units, and instrumentalities. Bonds issued by PBA to finance such facilities are payable from lease collections, which are largely derived from Commonwealth appropriations and are further secured by the Commonwealth's guaranty.

***Puerto Rico Maritime Shipping Authority (PRMSA)*** – PRMSA is governed by the President of the Government Development Bank for Puerto Rico (GDB). The operations of PRMSA consist of servicing the long-term liability to third parties that resulted from the sale of certain maritime operations formerly owned and operated by PRMSA. The Commonwealth is required to annually appropriate funds in its general operating budget to provide for the payment of principal and interest on such debt [see note 14 (d)].

***The Children's Trust (the Trust)*** – The Trust is governed by a seven-member board comprised by the Governor, who is the Chairman, the President of GDB, the Director of the Office of Management and Budget (OMB) of the Commonwealth, the Secretary of Justice of the Commonwealth, and three private citizens appointed by the Governor with the consent of the Senate. The Trust's sole operation consists of providing financial assistance principally to the Commonwealth's departments to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico, especially in the areas of education, recreation, and health. The operation of the Trust is financed with the moneys being received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

Complete financial statements of the blended component units can be obtained directly by contacting their respective administrative offices at:

Public Buildings Authority  
P.O. Box 41029 Minillas Station  
San Juan, PR 00940-1029

The Children's Trust  
P.O. Box 42001  
San Juan, PR 00940-2001

Puerto Rico Maritime Shipping Authority  
P.O. Box 362829  
San Juan, PR 00936-2829

#### ***Discretely Presented Component Units***

The following component units, consistent with GASB No. 14, are discretely presented in the financial statements because of the nature of the services they provide and the Commonwealth's ability to impose its will. These have been classified by management between major and nonmajor component units.

#### **Major Component Units**

***GDB*** – GDB is governed by a seven-member board appointed by the Governor. GDB acts as fiscal agent, depository of funds, disbursing agent, and financial advisor for the Commonwealth, its public corporations, and municipalities in connection with the issuance of bonds and notes; and it also makes loans and advances funds predominantly to public corporations and the Commonwealth's municipalities.

***Puerto Rico Highway and Transportation Authority (PRHTA)*** – PRHTA is governed by the Secretary of the DTPW. PRHTA has broad powers to carry out its responsibilities in accordance with DTPW's overall transportation policies. These powers include, among other things, the complete control and supervision of any highway facilities constructed, owned, or operated by PRHTA, the ability to set tolls for the use of the highway facilities, and the power to issue bonds, notes, or other obligations. PRHTA plans and manages the construction of all major projects relating to the Commonwealth toll highway system, undertakes major repairs, and maintains the toll ways.

***Puerto Rico Electric Power Authority (PREPA)*** – PREPA is governed by a nine-member board. Seven members are appointed by the Governor with the advice and consent of the Senate, and the remaining two members represent the consumers' interest and are elected in a referendum carried out by the Puerto Rico Consumer Affairs Department. Board members are appointed or elected for a period of four years. PREPA is responsible for conserving, developing, and utilizing the power resources of Puerto Rico and owns and operates the Commonwealth's electrical power generation and distribution system.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

***Puerto Rico Aqueduct and Sewer Authority (PRASA)*** – PRASA is governed by a nine-member board composed by five members appointed by the Governor, the Secretary of DTPW, the President of GDB, and two members elected in a referendum carried out by the Puerto Rico Consumer Affairs Department. PRASA owns and operates the system of public water supply and sanitary sewer facilities. PRASA is authorized, among other things, to borrow money and issue revenue bonds for any of its corporate purposes. Through the approval of Act No. 328 of 1998, as discussed in note 15 (a), the Commonwealth guarantees the principal and interest payments of certain outstanding bonds and of all future bonds issued to refinance those outstanding bonds, and other loans under the State Revolving Fund Program. PRASA has maintained privatization contracts for the administration of its operations since 1985. As disclosed in note 20 (d), in January 2004 and in April 2004, the operation, management, repair, and maintenance of the PRASA systems returned to PRASA.

***Puerto Rico Infrastructure Financing Authority (PRIFA)*** – PRIFA is governed by the board of directors of GDB and the Secretary of the Treasury of the Commonwealth. Its responsibilities are to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other component units and governmental instrumentalities of the Commonwealth, which are authorized to develop infrastructure facilities and to establish alternate means for financing them.

***Puerto Rico Health Insurance Administration (PRHIA)*** – PRHIA is governed by a seven-member board comprised of the Secretary of Health of the Commonwealth, the Secretary of the Treasury of the Commonwealth, the Insurance Commissioner of Puerto Rico, and four additional members appointed by the Governor, with the consent of the Senate, including two professionals with competence in the insurance industry and health services, and two representing the public interest. PRHIA was created for implementing, administering, and negotiating a health insurance system through contracts with insurance underwriters to provide quality medical and hospital care to low-income individuals.

***University of Puerto Rico (UPR)*** – UPR is governed by a nine-member board of trustees comprised of the Secretary of Education of the Commonwealth and eight members, including one full-time student and two professors, representing the public interest in higher education that are appointed by the Governor with the advice and consent of the Senate. Board members are appointed for a period of six years. The terms for the student and professors are of one year.

#### **Nonmajor Component Units**

***Agricultural Services and Development Administration (ASDA)*** – ASDA is governed by the Secretary of Agriculture of the Commonwealth. The purpose of ASDA is to provide a wide variety of services and incentives to the agricultural sector.

***Automobile Accident Compensation Administration (AACA)*** – AACA is governed by a five-member board comprised of one member of the Cabinet of the Governor and four members appointed by the Governor with the advice and consent of the Senate. AACA operates a system of compulsory insurance coverage for all registered motor vehicles and compensates citizens for injuries arising from motor vehicle accidents.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

***Caribbean Basin Projects Financing Authority (CBPFA)*** – CBPFA is governed by a seven-member board consisting of the Secretary of State of the Commonwealth, the Economic Development Administrator, the President of GDB, the President of Economic Development Bank for Puerto Rico and three citizens, including at least two from the private sector, appointed by the Governor with the advice and consent of the Senate. CBPFA is authorized to issue revenue bonds and to loan the proceeds thereof to finance projects for the development of the Caribbean Basin countries that were authorized to receive investments of funds under the provisions of Section 936 of the U.S. Internal Revenue Code.

***Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico (CDASFIPR)*** – CDASFIPR is governed by an eleven-member board of directors comprised, among others, of the Secretary of Economic Development and Commerce, the Chairman of the Board of the Puerto Rico Public Broadcasting Corporation, the Secretary of the Treasury of the Commonwealth, the Executive Director of the Institute of Puerto Rican Culture (IPRC), and three private citizens, appointed by the Governor with the advice and consent of the Senate. At least two of these private citizens must have proven interest, knowledge, and experience in arts, sciences, and the film industry. CDASFIPR was created with the purpose of developing the production of local films in Puerto Rico.

***Economic Development Bank for Puerto Rico (EDB)*** – EDB is governed by a nine-member board comprised of the President of GDB, who is the Chairman, the Secretary of Agriculture of the Commonwealth, an officer from the Department of Economic Development and Commerce, the Executive Director of the Puerto Rico Industrial Development Company, the Executive Director of the Tourism Company of Puerto Rico, and four other members representing the private sector and appointed by the Governor with the consent of the Senate. Private sector members are appointed for a period of three years. EDB is responsible for the promotion and development of the private sector economy of the Commonwealth. This purpose is to be met by granting direct loans, loan guarantees, and/or direct investments to any person or business organization devoted to manufacturing, agriculture, trade, tourism, or other service enterprises with preference but not limited to economic activities that may have the effect of substituting imports.

***Employment and Training Enterprises Corporation (ETEC)*** – ETEC is governed by a ten-member board comprised of the Puerto Rico Corrections Administrator, the Administrator of Youth Correctional Institutions, the Secretary of Justice of the Commonwealth, the Secretary of Education of the Commonwealth, the Executive Director of the Right to Employment Administration, the Administrator of the Administration of Mental Health and Anti-Addiction Services, the Sub-Administrator for the Promotion of Puerto Rico Industries of the Economic Development Administration, the Director of the Volunteer Corps, and two private citizens appointed by the Governor with the consent of the Senate. The purpose of ETEC is to provide training, management, development, and employment for inmates of the correctional institutions of the Commonwealth.

***Farm Insurance Corporation of Puerto Rico (FICPR)*** – FICPR is governed by a five-member board consisting of the Secretary of Agriculture of the Commonwealth, the Dean of the Agriculture Sciences Faculty of the UPR Mayagüez Campus, a representative of GDB, and two bona fide

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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farmers appointed by the Governor with the consent of the Senate. The purpose of the FICPR is to provide insurance to farmers against losses in their farms caused by natural disasters.

***Fine Arts Center Corporation (FACC)*** – FACC is governed by the board of directors of the IPRC. FACC was created with the purpose of administering the Fine Arts Center.

***Governing Board of the 9-1-1 Service (911 Service)*** – The Governing Board of 9-1-1 Service (the Board) is comprised of the Commissioner of Security and Public Protection, the Executive Director of the Medical Emergency Services, the Director of the State Emergency Management Agency, the Chief of the Puerto Rico Firefighters Corps, and one member appointed by consensus of the four ex-official members to represent the public interest. The 911 Service is responsible for providing an efficient service of fast response to emergency calls through the 9-1-1 number and transferring these to the appropriate response agencies using technological and human resources to safeguard lives and properties.

***Land Authority of Puerto Rico (LAPR)*** – LAPR is governed by a five-member board consisting of the Secretary of Agriculture of the Commonwealth and four members appointed by the Governor with the consent of the Senate. LAPR was created to carry out the provisions of the Land Law of Puerto Rico.

***Musical Arts Corporation (MAC)*** – MAC is governed by a seven-member board appointed by the Governor with the consent of the Senate including the president of the board of IPRC. MAC was created to promote the development of the arts and cultural programs of the Commonwealth.

***National Parks Company of Puerto Rico (NPCPR)*** – NPCPR is governed by a nine-member board comprised of the Secretary of Recreation and Sports of the Commonwealth (the Secretary), who is the chairman, the Secretary of Education of the Commonwealth, the Executive Director of the Tourism Company of Puerto Rico (TCPR), the Secretary of Natural and Environmental Resources of the Commonwealth, or any officer appointed by their respective agencies, and five members appointed by the Governor with the recommendation from the Secretary and with known interest in the development and preservation of parks in the private sector. NPCPR is responsible for the operation of all national parks and the protection, conservation, and use of parks, beaches, forests, natural, and historical monuments for the optimum enjoyment of present and future generations.

***Public Corporation for the Supervision and Deposit Insurance of Puerto Rico Cooperatives (PCSDIPRC)*** – PCSDIPRC (formerly the Corporation of Stock and Deposit Insurance for the Savings and Loans Cooperatives) is governed by a nine-member board consisting of the Commissioner of Financial Institutions of Puerto Rico (the Commissioner of Financial Institutions), the Insurance Commissioner of Puerto Rico, the Administrator of the Cooperative Development Administration, the Secretary of the Treasury of the Commonwealth, the Director of OMB, the President of GDB, two citizens representing the cooperative movement, and one private citizen representing the public interest. PCSDIPRC has the responsibility of providing to all the cooperatives and the Federation of Cooperatives of Puerto Rico, insurance coverage over the stocks and deposits, for monitoring the financial condition of the insured cooperatives, and of uninsured cooperatives when requested by the Commissioner of Financial Institutions.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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***Puerto Rico and Caribbean Cardiovascular Center Corporation (PRCCCC)*** – PRCCCC is governed by a five-member board comprised of the Secretary of Health of the Commonwealth, the Director of the Medical Sciences Campus of the UPR, the Executive Director of the Puerto Rico Medical Services Administration, and two additional members appointed by the Governor with the consent of the Senate, one of which should be from the Cardiology Society of Puerto Rico and another a member of a cardiology foundation properly registered in the Department of State of the Commonwealth. The purpose of the PRCCCC is to provide special treatment to patients suffering from cardiovascular diseases.

***Puerto Rico Conservatory of Music Corporation (PRCMC)*** – PRCMC is governed by a seven-member board appointed by the Governor. PRCMC is responsible for providing the Puerto Rican community and especially its youths with the required facilities to educate and perfect their musical skills, including secondary education programs for developing musical arts. It prepares the artistic element that nourishes the Puerto Rico Symphony Orchestra and other musical organizations, and coordinates the governmental efforts to interested industries, private enterprises, and particular citizens.

***Puerto Rico Convention Center District Authority (PRCCDA)*** – PRCCDA is governed by a board comprised of nine members, three of which shall be from the public sector and six of which shall be from the private sector. The public sector members are comprised of the Secretary of Economic Development and Commerce of the Commonwealth, who is the Chairman, the Executive Director of the Puerto Rico Tourism Company, and the Mayor of the Municipality of San Juan. The private sector members are individuals having experience in the areas of hospitality, tourism, real estate, or convention centers who are appointed by the Governor with the advice and consent of the Senate. PRCCDA was created to develop, own, finance, plan, design, construct, operate, manage, and promote the new Puerto Rico Convention Center, currently under development.

***Puerto Rico Council on Higher Education (PRCHE)*** – PRCHE is governed by a board comprised of eight members appointed by the Governor with the advice and consent of the Senate and the Secretary of Education of the Commonwealth as an ex-officio member. Its purpose is to develop higher education, to administer the licensing and certification of institutions of higher education and to administer scholarship funds.

***Puerto Rico Exports Development Corporation (PREDC)*** – PREDC is governed by the board of GDB. PREDC's purpose is to encourage the economic development of Puerto Rico by promoting the export of products and services of Puerto Rico to other countries and maintaining commercial facilities for lease to the public and private sector.

***Puerto Rico Government Investment Trust Fund (PRGITF)*** – PRGITF is governed by the Secretary of the Treasury of the Commonwealth. GDB is its trustee, custodian, and administrator. PRGITF's main objective is to provide investment opportunities in a professionally managed money market portfolio by investing, in high quality securities, with minimal credit risk. Qualified investors include the Commonwealth's central government, its public corporations, instrumentalities and agencies, and the municipalities of Puerto Rico. In conformity with GASB Statement No. 31,

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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*Accounting and Financial Reporting for Certain Investments and for External Investments Pools*, the financial statements of the PRGITF are not included in the accompanying basic financial statements because each primary government and component unit investor is already presenting as cash or investment their corresponding share of the assets of the PRGITF (see note 4).

***Puerto Rico Industrial Development Company (PRIDCO)*** – PRIDCO is governed by a seven-member board comprised of the Secretary of Economic Development and Commerce of Puerto Rico, who is the Chairman, the Secretary of the Treasury of the Commonwealth, the President of GDB, the President of the Planning Board of Puerto Rico, and three members from the private sector appointed by the Governor with the advice and consent of the Senate. The private sector members are appointed for a period of four years. PRIDCO administers the Commonwealth-sponsored economic development program by providing facilities, general assistance, and special incentive grants to manufacturing companies operating in Puerto Rico. PRIDCO has issued interim notes and revenue bonds to finance manufacturing plants and other facilities. Rentals derived from the leasing of specified facilities of PRIDCO are pledged for the payment of PRIDCO's revenue bonds.

***Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority (known as AFICA by its Spanish acronym)*** – AFICA is governed by a seven-member board consisting of the Economic Development Administrator, the President of GDB, the Executive Director of PRASA, the Executive Director of the Tourism Company of Puerto Rico, the President of the Environmental Quality Board, and two private citizens appointed by the Governor. AFICA is authorized to issue revenue bonds to finance industrial, tourist, environmental control, medical, and educational facilities in Puerto Rico and the United States for use by private companies, nonprofit entities, or governmental agencies. The bonds are payable solely from collections from such private companies, nonprofit entities, or governmental agencies, and do not constitute debt of the Commonwealth or any of its other component units.

***Puerto Rico Land Administration (PRLA)*** – PRLA is governed by an eleven-member board comprised of the Governor of Puerto Rico, who serves as president, the Secretary of the Treasury of the Commonwealth, the Secretary of Agriculture of the Commonwealth, the Secretary of DTPW of the Commonwealth, the Secretary of Housing of the Commonwealth, the Economic Development Administrator, the President of the Planning Board, and four other members appointed by the Governor with the advice and consent of the Senate. PRLA acquires parcels of land on behalf of government instrumentalities through negotiation or expropriation.

***Puerto Rico Maritime Transportation Authority (PRMTA)*** – PRMTA is under the control of the Secretary of DTPW of the Commonwealth. Its purpose is to administer and operate the maritime transportation services (ferries operations) formerly operated by the Puerto Rico Ports Authority.

***Puerto Rico Medical Services Administration (PRMSA)*** – PRMSA is governed by a ten-member board comprised of the Secretary of Health of the Commonwealth, who is the Chairman, the Dean of the Medical Sciences Faculty of the UPR, the President of Board of the Puerto Rican Cancer Society, the Mayor of the Municipality San Juan, the Administrator of the State Insurance Fund Corporation (SIFC), the Secretary of the Department of Family Affairs of the Commonwealth, the Administrator of the Administration of Mental Health and Anti-Addiction Services, the President of

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

the Medical Policy and Administration Committee, and two consumers appointed by the Secretary of Health of the Commonwealth. Its purpose is to plan, organize, operate, and administer the centralized health services, provided in support of the hospital and other functions offered by the member institutions and users of the medical complex known as the Puerto Rico Medical Center.

***Puerto Rico Metropolitan Bus Authority (PRMBA)*** – PRMBA is governed by the Secretary of Transportation and Public Works of the Commonwealth. PRMBA provides transportation to passengers within the San Juan Metropolitan Area. This service is financed by Commonwealth and federal government appropriations and passenger fares.

***Puerto Rico Municipal Finance Agency (PRMFA)*** – PRMFA is governed by a five-member board comprised of the President of GDB, who is the Chairman, Commissioner of Municipal Affairs, and three additional members appointed by the Governor, one of whom shall be either the mayor or chief financial officer of a municipality. PRMFA was organized to create a capital market to assist the municipalities of Puerto Rico in financing their public improvement programs.

***Puerto Rico Ports Authority (PRPA)*** – PRPA is governed by a five-member board consisting of the Secretary of DTPW of the Commonwealth, who is the Chairman, the Secretary of Economic Development and Commerce of the Commonwealth, the Economic Development Administrator, the Executive Director of the Tourism Company of Puerto Rico, and one private citizen appointed for a period of four years by the Governor with the advice and consent of the Senate. The purpose of PRPA is to administer all ports and aviation transportation facilities of the Commonwealth and to render other related services.

***Puerto Rico Public Broadcasting Corporation (PRPBC)*** – PRPBC is governed by an eleven-member board of directors comprised of the Secretary of Education of the Commonwealth, the President of the UPR, the Executive Director of IPRC, and eight private citizens, appointed by the Governor with the advice and consent of the Senate. At least three of these private citizens must have proven interest, knowledge, and experience in education, culture, art, science, or radio and television. PRPBC was created with the purpose of integrating, developing, and operating the radio, television, and electronic communication facilities that belong to the Commonwealth.

***Puerto Rico School of Plastic Arts (PRSPA)*** – PRSPA is governed by a seven-member board. Four members are appointed by the board of directors of IPRC, representing the public educational and cultural interests. Board members may not be employees of the PRSPA. The remaining three members are elected from among the members of the board of directors of IPRC, one of whom will serve as president. PRSPA was created to develop, promote, plan, and coordinate programs of study in higher education oriented to the plastic arts, teaching artistic techniques, and to help students to develop humanistic values.

***Puerto Rico Solid Waste Authority (PRSWA)*** – PRSWA is governed by an eleven-member board appointed by the Governor with the advice and consent of the Senate. PRSWA provides alternatives for processing of solid waste and encourages recycling, reuse, and recovery of resources from waste.



## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

***Puerto Rico Telephone Authority (PRTA)*** – PRTA is governed by a five-member board comprised of the President of GDB and four members that are appointed by the board of directors of GDB. PRTA is the legal entity responsible to account for the equity interest in Telecomunicaciones de Puerto Rico, Inc. for the benefit of the Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities.

***Right to Employment Administration (REA)*** – REA is governed by an administrator appointed by the Governor with the consent of the Senate. In addition, a consultative board comprised of the Secretary of Labor of the Commonwealth, the Secretary of Agriculture of the Commonwealth, the Secretary of Transportation and Public Works of the Commonwealth, the Secretary of Education of the Commonwealth, and five additional members appointed by the Governor, with the consent of the Senate, will advise the administrator on the implementation of the Right to Employment Act.

***Special Communities Perpetual Trust (SCPT)*** – SCPT was created through Act 271 of November 21, 2002. It is governed by a board of directors composed of seven members: the Secretary of Housing of the Commonwealth, the Secretary of Transportation and Public Works of the Commonwealth, the Coordinator for the Social and Economic Financing of the Special Communities, one mayor of a municipality of Puerto Rico, one community leader resident in one special community and two private citizens representing the public interest. All members of the board of directors are appointed by the Governor. SCPT's principal purpose is to fund development projects which address the infrastructure and housing needs of underprivileged communities. SCPT's capital will consist of moneys drawn under a \$500 million GDB line of credit, which is currently in use by SCPT, and a \$500 million grant from GDB to be disbursed over time after the line of credit has been fully disbursed.

***State Insurance Fund Corporation (SIFC)*** – SIFC is governed by a seven-member board appointed by the Governor with the advice and consent of the Senate. The board is comprised by the Commissioner of Insurance of Puerto Rico, an officer from the Department of Labor and Human Resources of the Commonwealth, an officer from the Department of Health of the Commonwealth, a representative of the employees' interest, a representative of the employees' interest, and two members without any of these interests. Members are appointed for a period of six years. SIFC provides workers' compensation and disability insurance to public and private employees.

***TCPR*** – TCPR is governed by a seven-member board comprised of representatives of different tourist-related sectors appointed by the Governor with the consent of the Senate. At least one member must represent internal tourism and two must not be residents of the metropolitan area. Its purpose is to promote the tourism industry of Puerto Rico.

## COMMONWEALTH OF PUERTO RICO

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Complete financial statements of the discretely presented component units can be obtained directly by contacting their administrative offices:

Government Development Bank for Puerto Rico P.O. Box 42001 San Juan, PR 00940-2001	Puerto Rico Highway and Transportation Authority P.O. Box 42007 San Juan, PR 00940-2007
Puerto Rico Electric Power Authority P.O. Box 364267 San Juan, PR 00936-4267	Puerto Rico Aqueduct and Sewer Authority P.O. Box 7066 San Juan, PR 00916-7066
Puerto Rico Infrastructure Financing Authority P.O. Box 42001 San Juan, PR 00940-2001	Puerto Rico Health Insurance Administration P.O. Box 4264 San Juan, PR 00902-4264
University of Puerto Rico P.O. Box 364984 San Juan, PR 00936-4984	Agricultural Services and Development Administration P.O. Box 9200 San Juan, PR 00908-0202
Automobile Accident Compensation Administration P.O. Box 364847 San Juan, PR 00936-4847	Caribbean Basin Projects Financing Authority P.O. Box 42001 San Juan, PR 00940-2001
Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico P.O. Box 362350 San Juan, PR 00936-2350	Economic Development Bank for Puerto Rico P.O. Box 2134 San Juan, PR 00922-2134
Employment and Training Enterprises Corporation P.O. Box 366505 San Juan, PR 00936-6505	Farm Insurance Corporation of Puerto Rico P.O. Box 9200 San Juan, PR 00908-0200
Fine Arts Center Corporation P.O. Box 41287 – Minillas Station Santurce, PR 00940-1287	Governing Board of the 9-1-1 Service P.O. Box 27020 San Juan, PR 00927-0200
Land Authority of Puerto Rico P.O. Box 9745 San Juan, PR 00908-9745	Musical Arts Corporation P.O. Box 41227 – Minillas Station San Juan, PR 00940-1227

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National Parks Company of Puerto Rico  
P.O. Box 9022089  
San Juan, PR 00902-2089

Puerto Rico and Caribbean  
Cardiovascular Center Corporation  
P.O. Box 366528  
San Juan, PR 00936-6528

Puerto Rico Convention Center District  
Authority  
P.O. Box 19269  
San Juan, P.R 00910-1269

Puerto Rico Exports Development  
Corporation  
P.O. Box 195009  
San Juan, PR 00936-5009

Puerto Rico Industrial Development  
Company  
P.O. Box 362350  
San Juan, PR 00936-2350

Puerto Rico Land Administration  
P.O. Box 363767  
San Juan, PR 00936-3767

Puerto Rico Medical Services  
Administration  
P.O. Box 2129  
San Juan, PR 00922-2129

Puerto Rico Municipal Finance Agency  
P.O. Box 42001  
San Juan, PR 00940-2001

Puerto Rico Public Broadcasting Corporation  
P.O. Box 190-0909  
San Juan, PR 00919-0909

Puerto Rico Solid Waste Authority  
P.O. Box 40285 – Minillas Station  
San Juan, PR 00940-0285

Public Corporation for the Supervision and  
Deposit Insurance of Puerto Rico Cooperatives  
P.O. Box 195449  
San Juan, PR 00919-5449

Puerto Rico Conservatory of Music Corporation  
350 Lamar Street and Roosevelt Avenue  
San Juan, PR 00918-2199

Puerto Rico Council on Higher Education  
P.O. Box 19900  
San Juan, PR 00910-1900

Puerto Rico Government Investment Trust Fund  
P.O. Box 42001 – Minillas Station  
San Juan, PR 00940-2001

Puerto Rico Industrial, Tourist, Educational,  
Medical, and Environmental Control Facilities  
Financing Authority  
P.O. Box 42001 – Minillas Station  
San Juan, PR 00940-2001

Puerto Rico Maritime Transportation Authority  
P.O. Box 362829  
San Juan, PR 00940-2829

Puerto Rico Metropolitan Bus Authority  
P.O. Box 195349  
San Juan, PR 00919-5349

Puerto Rico Ports Authority  
P.O. Box 362829  
San Juan, PR 00936-2829

Puerto Rico School of Plastic Arts  
P.O. Box 9021112  
San Juan, PR 00902-1112

Puerto Rico Telephone Authority  
P.O. Box 360998  
San Juan, PR 00936-0098

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Right to Employment Administration  
P.O. Box 364452  
San Juan, PR 00936-4452

State Insurance Fund Corporation  
P.O. Box 365028  
San Juan, PR 00936-5028

Special Communities Perpetual Trust  
P.O. Box 42001  
San Juan, PR 00940-2001

Tourism Company of Puerto Rico  
P.O. Box 902-3960  
Old San Juan Station  
San Juan, PR 00902-3960

The financial statements of the discretely presented component units have a year-end of June 30, 2003 except for the Puerto Rico Telephone Authority, which has a year-end of December 31, 2002.

#### **Fiduciary Component Units**

The three employee retirement systems administer pension funds for the Commonwealth and its political subdivisions. The three systems are subject to legislative and executive controls and the administrative expenses are subject to legislative budget controls. These component units, while meeting the definition of a component unit and are legally separate, are presented in the fund financial statements along with other fiduciary funds of the Commonwealth. They have been omitted from the government-wide financial statements.

#### ***Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS)***

– ERS is governed by a board of trustees, which is composed of the Secretary of the Treasury of the Commonwealth, who is the President, the President of GDB, the Insurance Commissioner of Puerto Rico, the Director of the Puerto Rico Central Office of Personnel Administration, two participating employees, and one retiree, who are appointed by the Governor. The Commonwealth reports ERS as a single-employer pension plan. ERS is the administrator of a defined-benefit pension plan, which covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and component units not covered by their own retirement systems. On September 24, 1999, an amendment to the law that created ERS was enacted with the purpose of establishing a new defined-contribution plan (System 2000) for employees hired by the government on or after January 1, 2000.

***Puerto Rico Judiciary Retirement System (JRS)*** – JRS is governed by the same board of trustees as ERS. JRS is a single-employer defined-benefit plan, administered by ERS, which covers all individuals holding a position as Justice of the Supreme Court, Judge of the Superior Court or the District Court, or Municipal Judges of the Commonwealth.

***Puerto Rico System of Annuities and Pensions for Teachers (TRS)*** – TRS is governed by a five-member board comprised of the Secretary of Education of the Commonwealth, the Secretary of the Treasury of the Commonwealth, the President of GDB and two participating members (one of whom is a retiree and the other the president of one of the teachers' organizations) appointed by the Governor with the advice and consent of the Senate for four years. The Commonwealth reports TRS

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as a single-employer pension plan. TRS provides retirement benefits to all teachers of the Department of Education of the Commonwealth, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education of the Commonwealth, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education of the Commonwealth. TRS provides retirement, death, and disability benefits.

Complete financial statements of these component units can be obtained directly by contacting their respective administrative offices at:

Employees' Retirement System of the  
Government of Puerto Rico and its  
Instrumentalities  
P.O. Box 42003 – Minillas Station  
Santurce, PR 00940

Puerto Rico Judiciary Retirement System  
P.O. Box 42003 – Minillas Station  
Santurce, PR 00940

Puerto Rico System of Annuities and Pensions for  
Teachers  
P.O. Box 1879  
San Juan, PR 00919-1879

#### (c) *Government-wide Financial Statements*

The government-wide financial statements (the statement of net assets and the statement of activities) report information of all of the nonfiduciary activities of the Commonwealth and its component units. For the most part, the effect of interfund activity has been removed from these government-wide financial statements. Governmental activities, which normally are supported by taxes and intergovernmental revenue, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable. The statement of net assets presents the reporting entities' nonfiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

- ***Invested in Capital Assets, Net of Related Debt*** – These consist of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- ***Restricted Net Assets*** – These result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.

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### Notes to Basic Financial Statements

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- ***Unrestricted Net Assets*** – These consist of net assets which do not meet the definition of the two preceding categories. Unrestricted net assets often are designated to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on resources that are imposed by management, but can be removed or modified.

When both restricted and unrestricted resources are available for use, generally it is the Commonwealth's policy to use restricted resources first, then the unrestricted resources as they are needed.

The statement of activities demonstrates the degree to which the direct expenses of a given function, segment, or component unit are offset by program revenue. Direct expenses are those that are clearly identifiable with a specific function, segment, or component unit. Program revenue includes charges to customers who purchase, use, or directly benefit from goods or services provided by a given function, segment, or component unit. Program revenue also includes grants and contributions that are restricted to meeting the operational or capital requirements of a particular function, segment, or component unit. Taxes and other items not properly included among program revenue are reported instead as general revenue. Resources that are dedicated internally are reported as general revenue rather than as program revenue. The Commonwealth does not allocate general government (indirect) expenses to other functions.

#### ***(d) Measurement Focus, Basis of Accounting, and Financial Statement Presentation***

***Government-wide Financial Statements*** – The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements have been met.

***Governmental Fund Financial Statements*** – The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available when it is collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Commonwealth considers most revenue to be available if collected within 120 days after the end of the current fiscal year-end. Principal revenue sources considered susceptible to accrual include tax revenue, net of estimated overpayments (refunds) and amounts considered not collectible, which are recorded as taxpayers earn income (income taxes), as sales are made (consumption and use taxes), and as cash is received (miscellaneous taxes). In applying the susceptible to accrual concept to federal grants, there are essentially two types of revenue. For the majority of grants, moneys must be expended by the Commonwealth on the specific purpose or project before any amounts will be reimbursed. Revenue is, therefore, recognized as expenditures are incurred to the extent available. For the other revenue, moneys are virtually unrestricted and are generally revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt

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or earlier if the susceptible to accrual criteria is met. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include the following:

- Employees' vested annual vacation and sick leave is recorded as expenditure when utilized. The amount of accumulated annual vacation and sick leave unpaid at June 30, 2003 has been reported only in the government-wide financial statements.
- Interest and principal on general long-term obligations are recorded when due, except for interest and principal due in July 1 of the following fiscal year.
- Executory purchase orders and contracts are recorded as a reservation of fund balance.
- Debt service expenditures, federal funds cost disallowances, other long-term obligations, and amounts subject to judgments under litigation are recorded only when payment is due.

***Proprietary Funds, Fiduciary Funds, and Discretely Presented Component Units Financial Statements*** – The financial statements of the proprietary funds, fiduciary funds and discretely presented component units are reported using the economic measurement focus and the accrual basis of accounting, similar to the government-wide financial statements described above.

Each proprietary fund has the option under GASB Statement No. 20 to elect and apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless these conflict with a GASB pronouncement. The primary government's major enterprise funds have elected not to apply FASB pronouncements issued after November 30, 1989 and two nonmajor enterprise funds elected to adopt the FASB's pronouncements issued after November 30, 1989. Also, certain discretely presented component units have disclosed their election in their separately issued financial statements. The component units follow GAAP as issued by GASB and FASB as applicable to each component unit based on the nature of their operations. In addition, the Puerto Rico Government Investment Trust Fund adopted GASB Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investments Pools*, however, such financial statements are not included in the accompanying basic financial statements because each primary government and the component units investor already present their corresponding share of the assets of the PRGITF as cash or investments.

Proprietary funds distinguish operating revenue and expenses from nonoperating items. Operating revenue and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. Revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses. The major operating revenue of the Commonwealth enterprise funds is as follows:

- ***Unemployment Insurance Trust Fund*** – Amounts requisitioned for the Puerto Rico Unemployment Insurance Trust Fund held by the U.S. Treasury for payment of unemployment benefits and charges made to individual employers.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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- **Lotteries Fund** – Amounts collected from the sale of traditional lottery tickets and electronic lotto games.

#### (e) **Fund Accounting**

The Commonwealth reports its financial position and results of operations in funds, which are considered separate accounting entities and discrete presentations of those component units which are not required to be blended. The operations of each fund are accounted for within a set of self-balancing accounts. Fund accounting segregates funds according to their intended purpose and is used to aid management in demonstrating compliance with legal, financial, and contractual provisions. Major funds are determined using a predefined percentage of the assets, liabilities, revenue, or expenditures/expenses of either the fund category or the governmental and enterprise funds combined. The nonmajor funds are combined in a single column in the fund financial statements. The Commonwealth reports the following major funds:

#### **Governmental Funds**

**General Fund** – The general fund is the primary operating fund of the Commonwealth. It is used to account for all financial transactions, except those required to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, and education.

**Debt Service Fund** – The debt service fund accounts for the accumulation of resources predominantly for, and the payment of, general long-term bonds' principal, interest and related costs other than bonds payable from the operations of proprietary fund types, pension trust funds and discretely presented component units. Long-term debt and interest due on July 1 of the following fiscal year are accounted for as a fund liability if resources are available as of June 30 for its payment.

**Public Buildings Authority Capital Projects Fund** – The Public Buildings Authority's capital projects fund is used to account for the financial resources used for the acquisition or construction of major capital facilities not financed by proprietary fund types, pension trust funds, and discretely presented component units.

**The Children's Trust Special Revenue Fund** – The Children's Trust special revenue fund is used to account for the moneys received by the Commonwealth from a global settlement agreement dated November 23, 1998, between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The financial resources received by this fund are used to carry out projects aimed at promoting the well-being of children and youth of Puerto Rico.

#### **Proprietary Funds**

These funds account for those activities for which the intent of management is to recover, primarily through user charges the cost of providing goods or services to the general public.



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***Unemployment Insurance Trust Fund*** – This fund accounts for amounts requisitioned for the Puerto Rico Unemployment Insurance Trust Fund held by the U.S. Treasury for payment of unemployment benefits and charges made to individual employers.

***Lotteries Fund*** – This fund accounts for the assets and operations of two lottery systems administered by the Commonwealth.

#### **Fiduciary Funds**

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity, or as an agent for individuals, private organizations, and other governmental units. The following are the Commonwealth's fiduciary funds:

***Pension Trust Funds*** – are used to account for the assets, liabilities, and net assets available for pension benefits held in trust for the public employees' retirement systems.

***Agency Funds*** – are custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

#### **Discretely Presented Component Units**

Discrete presentation of component units is used to present the financial information of entities that do not qualify to be blended, in accordance with GASB No. 14, with the funds of the primary government. The component units column in the government-wide financial statements is used to report the financial activities of the Commonwealth's discretely presented component units. The financial statements of these component units are presented following the accrual basis of accounting. Under the accrual basis, revenue is recognized when earned and expenses are recorded as liabilities when incurred, without regard to receipt or payment of cash.

#### **(f) Statutory (Budgetary) Accounting**

The Commonwealth's budget is adopted in accordance with a statutory basis of accounting, which is not in accordance with GAAP. Revenue is generally recognized when cash is received, net of tax refunds claimed by taxpayers as of year-end. Short- and long-term borrowings may be used to finance budgetary excess of expenditures over revenue. Expenditures are generally recorded when the related expenditure is incurred or encumbered. Encumbrances lapse the year following the end of the fiscal year when the encumbrance was established, as established by Act No. 123 of August 17, 2001, which amended the then existing appropriations and encumbrances lapsing provisions of Act No. 230 of July 23, 1974. Unencumbered appropriations lapse at year-end. Amounts required for settling claims and judgments against the Commonwealth, and certain other liabilities are not recognized until they are encumbered or otherwise processed for payment.

## COMMONWEALTH OF PUERTO RICO

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Under the statutory basis of accounting, the Commonwealth uses encumbrance accounting to record the full amount of purchase orders, contracts, and other commitments of appropriated resources as deductions from the appropriation prior to actual expenditure. In the governmental funds, encumbrance accounting is a significant aspect of budgetary control.

The statement of revenue and expenditures – budget and actual – budget basis – general fund, only presents the information for the general fund for which there is a legally adopted budget, as required by GAAP. See note 3 for a reconciliation of the statement of revenue and expenditures – budget and actual – budget basis – general fund with the statement of revenue, expenditures, and changes in fund balance (deficit) for the general fund.

#### **(g) *Cash and Short-Term Investments***

The Commonwealth follows the practice of pooling cash. The balance in the pooled cash accounts is available to meet current operating requirements and any excess is invested in various interest-bearing accounts with GDB, and with the PRGITF. At June 30, 2003, excess of checks drawn over the pooled bank balance amounted to \$91 million and is reported within accounts payable and accrued liabilities of the governmental activities.

Cash and cash equivalents include investments with original maturities of 90 days or less for the purpose of reporting enterprise fund cash flows.

The Commissioner of Financial Institutions requires that private financial institutions deposit collateral securities to secure the deposits of the Commonwealth and all other governmental entities in each of these institutions. The amount of collateral securities to be pledged for the security of public deposits shall be established by rules and regulations promulgated by the Commissioner of Financial Institutions.

The Puerto Rico Unemployment Insurance Trust Fund is maintained to account for the collection of unemployment insurance contributions from employers and the payment of unemployment benefits to eligible claimants. As required by federal law, all resources not necessary for current benefit payments are placed on deposit with the U.S. Treasury. Interest from these resources is retained in the fund.

Cash and short-term investments and cash equivalents of the component units are maintained in separate bank accounts, from those of the primary government, in their own names.

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**(h) *Securities Purchased Under Agreements to Resell***

Certain component units of the Commonwealth enter into purchases of securities with simultaneous agreements to resell. The amounts advanced under these agreements generally represent short-term loans and are reflected as an asset. The securities underlying these agreements mainly consist of U.S. government obligations, mortgage-backed securities, and interest-bearing deposits with other banks.

**(i) *Securities Lending Transactions***

Certain component units of the Commonwealth enter into securities lending transactions in which governmental entities (lenders) transfer their securities to broker-dealers and other entities (borrowers) for collateral with a simultaneous agreement to return the collateral for the same securities in the future. Securities received as collateral are generally reflected as investments with a corresponding liability resulting from the obligation to return such collateral.

**(j) *Investments***

Investments include U.S. government and agencies obligations, mortgage-backed securities, repurchase agreements, commercial paper, local government obligations, investment contracts, and corporate debt and equity obligations. Investment securities are presented at fair value, except for money market investments and participating investment contracts with a remaining maturity at the time of purchase of one year or less and nonparticipating investment contracts, which are presented at cost. Changes in the fair value of investments are presented as investment earnings in the statement of activities, the statement of revenue, expenditures, and changes in fund balance – governmental funds, and the statement of revenue, expenses, and changes in fund net assets – proprietary funds. Fair value is determined based on quoted market prices. When securities are not listed on national exchanges, quotations are obtained from brokerage firms.

The PRGIF is considered a 2a7-like external investment pool, and as such, reports its investments at amortized cost.

The reverse repurchase agreements reported by certain discretely presented component units were authorized transactions under their respective enabling legislation and authorized by GDB.

**(k) *Receivables***

Tax receivables in the general fund include predominantly amounts owed by taxpayers for individual and corporate income taxes, net of estimated uncollectible amounts. A portion of these income tax receivables is recognized as revenue when they become measurable and available based on actual collections during the 120 days following the fiscal year-end related to tax returns due before year-end. Tax receivables also include amounts owed by taxpayers on income earned in periods prior to June 30, 2003, estimated to be collectible but not currently available, and thus are reported as deferred revenue. Unemployment, disability, and driver's insurance receivable in the enterprise funds are stated net of estimated allowances for uncollectible accounts.

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Taxes receivable also includes taxes that the Municipal Revenue Collection Center (CRIM, as per its Spanish acronym), a municipal corporation, is required to remit to the Commonwealth to be used by the Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth. The amount to be remitted is based on the special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation, which is levied by the Commonwealth but collected by CRIM on the Commonwealth's behalf [see note 14(c)].

Accounts receivable are stated net of estimated allowances for uncollectible accounts, which are determined, based upon past collection experience and current economic conditions. Intergovernmental receivables primarily represent amounts owed to the Commonwealth for reimbursement of expenditures incurred pursuant to federally funded programs.

The accounts receivable from nongovernmental customers of the component units are net of estimated uncollectible amounts. These receivables arise primarily from service charges to users. Accounts receivable from the primary government and other component units that arise from service charges do not have allowances for uncollectible accounts, as these are deemed fully collectible.

Loans of the general fund represent predominantly amounts owed by public corporations and municipalities for public insurance and rent paid by the general fund on their behalf.

The loans of the pension trust funds do not have allowances for uncollectible amounts since such loans are secured by mortgage deeds, plan members' contributions, and any unrestricted amounts remaining in escrow. Loans of the component units consist predominantly of loans to the primary government, other component units and municipalities, and do not have allowances for uncollectible accounts as those are deemed fully collectible. The remaining loans of the component units are to small and medium businesses, agricultural, and low-income housing loans from nongovernmental customers, and are presented net of estimated losses on such portfolios.

#### *(l) Inventories*

Generally, inventories are valued at cost and predominantly on the first-in, first-out basis. Governmental fund inventories are recorded as expenditures when purchased rather than capitalized as an asset. Only significant amounts of inventory at the end of the year are capitalized in the governmental funds. However, inventories are always capitalized in the statement of net assets of governmental activities.

#### *(m) Restricted Assets*

Funds set aside for the payment and guarantee of notes and interest payable and for other specified purposes are classified as restricted assets since their use is limited for this purpose by applicable agreements or required by law. Restricted assets in the proprietary funds mainly include amounts set aside for the payment of lottery prizes.

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## Notes to Basic Financial Statements

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**(n) Real Estate Held for Sale**

Real estate held for sale is stated at their estimated net realizable value determined by management based on previous units sales, commitments, or appraisal values.

**(o) Capital Assets**

Capital assets, which include land, buildings, building improvements, equipment, vehicles, construction in process, and infrastructure assets are reported in the applicable governmental, business-type activities and component unit columns in the government-wide financial statements. The Commonwealth's primary government defines capital assets as assets, which have an initial, individual cost of \$25,000 or more at the date of acquisition and have a useful life of five or more years. Capital assets are recorded at historical cost or at estimated historical cost if actual historical cost is not available.

The method to deflate the current cost of the same or a similar asset using an approximate price index was used to estimate the historical cost of certain land, buildings, and building improvements because invoices and similar documentation was no longer available in certain instances. Donated capital assets are recorded at fair market value at the time of donation. Major outlays for capital assets and improvements are capitalized as projects are constructed. Interest costs are capitalized during construction period only for business-type activities and most component units. The costs of normal maintenance and repairs that do not add value to the assets or materially extend asset lives are not capitalized.

GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, provides transition standards that make available an extended period of deferral (fiscal year 2006) before the requirement to record and depreciate general infrastructure assets acquired before the implementation date (July 1, 2001) becomes effective. General infrastructure assets (such as, dams, intake facilities, and similar items) acquired prior to July 1, 2001 have not been recorded because capitalization information is not available. No new infrastructure expenditures have been made by governmental activities after implementation year.

Capital assets utilized in the governmental funds are recorded as expenditures in the governmental fund financial statements. Depreciation expense is recorded in the government-wide financial statements, as well as the proprietary funds and component units' financial statements.

Capital assets of the primary government are depreciated on the straight-line method over the assets' estimated useful life. There is no depreciation recorded for land and construction in progress. The estimated useful lives of capital assets are as follows:

	<u>Years</u>
Buildings and buildings improvements	20-50
Equipment, furniture, fixtures, and vehicles	5-15

# COMMONWEALTH OF PUERTO RICO

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The capital assets of the component units are recorded in accordance with the applicable standards of the component units and under their own individual capitalization thresholds. Depreciation has been recorded when required by these standards based on the types of assets, use and estimated useful lives of the respective assets, and on the nature of each of the component unit's operations.

The estimated useful lives of capital assets reported by the component units are as follows:

	<u>Years</u>
Buildings and buildings improvements	3-50
Equipment, furniture, fixtures, and vehicles	3-20
Infrastructure	10-50

**(p) Tax Refunds Payable**

During the calendar year, the Commonwealth collects individual income taxes through withholdings and payments from taxpayers. At June 30, the Commonwealth estimates the amount owed to taxpayers for overpayments during the first half of the calendar year. These estimated amounts and the actual tax refunds claimed for prior years but not paid at year-end are recorded as tax refunds payable and as a reduction of tax revenue.

**(q) Deferred Revenue**

Deferred revenue at the governmental fund level arises when potential revenue does not meet both the "measurable" and "available" criteria for revenue recognition in the current period. Deferred revenue also arises when resources are received before the Commonwealth has a legal claim to them, as when grant moneys are received prior to incurring the qualifying expenditures. In subsequent periods, when the revenue recognition criteria is met, or when the Commonwealth has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and the revenue is recognized. Deferred revenue at the government-wide and proprietary fund levels arises only when the Commonwealth receives resources before it has a legal claim to them.

**(r) Long-Term Debt**

The liabilities reported in the government-wide financial statements include Commonwealth general obligation bonds and long-term notes, obligations under lease/purchase agreements, and long-term liabilities including vacation, sick leave, long-term liabilities to other governmental entities, net pension obligation, legal claims, and noncurrent federal fund cost disallowances related to expenditures of federal grants. Long-term obligations financed by proprietary fund types and component units are recorded as liabilities in those funds and in the discretely presented component unit's column.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

***Premiums, Discounts, and Issuance Costs*** – In the government-wide financial statements, long-term debt, and other long-term obligations are presented in the columns for governmental and business-type activities. The same is presented in the proprietary fund financial statements. Bond and note premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the debt. Bonds and notes payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges in other assets and are amortized over the term of the related debt. In the governmental fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuance are reported as other financing sources while discounts are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as expenditures.

***(s) Reservations of Fund Balance – Governmental Funds***

The governmental fund financial statements present fund balance reserves for those portions of fund balance (1) not available for appropriation for expenditures or (2) legally segregated for a specific future use. The reserves for related assets such as inventories and prepayments are examples of the former. Reserves for encumbrances, debt service, and other specific purposes are examples of the latter.

***(t) Accounting for Pension Costs***

For the purpose of applying the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers* (GASB No. 27), the Commonwealth's financial reporting entity is considered to be a sponsor of three single-employer defined-benefit pension plans: ERS, JRS, and the TRS. This is because substantially all the participants in the three pension trust funds are part of the financial reporting entity of the Commonwealth. For the purpose of the basic financial statements, and as disclosed in note 19, the Commonwealth's annual pension cost, measured on the accrual basis of accounting, for the year ended June 30, 2003 amounted to approximately \$1 billion. However, the amount recognized as pension expenditure in the governmental funds was recorded under the modified accrual basis, and amounted to approximately \$460 million. The excess of the annual required contribution over the statutorily required contributions increased the net pension obligation at June 30, 2003 to approximately \$3.8 billion. This amount is presented in the statement of net assets of the governmental activities as of June 30, 2003.

For purposes of the stand-alone financial statements of each of the blended and discretely presented component units, the entities accounted for pension costs from the standpoint of a participant in a multiple-employer cost sharing plan. Accordingly, pension costs recognized are equal to the statutorily or contractually required contributions, with a liability recorded for any unpaid required contributions. The basis of accounting used by the component units was either modified accrual basis or accrual basis, depending upon individual fund structure and type of entity. Most component units did not have pension-related assets or liabilities at transition because they have contributed the statutorily required contributions.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

**(u) *Postemployment Benefits***

In addition to the pension benefits described in note 19, the Commonwealth provides postemployment healthcare benefits and a Christmas bonus for its retired employees in accordance with local law. Substantially all of the employees may become eligible for these benefits if they reach normal retirement age while working for the Commonwealth. Healthcare benefits are provided through insurance companies whose premiums are paid by the retiree with the Commonwealth providing a matching share of not more than \$60 per month for each retiree. During the year ended June 30, 2003, the cost of providing healthcare benefits amounted to approximately \$39 million for approximately 51,000 retirees. The Christmas bonus paid to the retired employees during the year ended June 30, 2003 was \$300 per retiree and the total amount was approximately \$26 million for approximately 85,000 retirees. These benefits are recorded as expenditures when paid in the general fund.

**(v) *Compensated Absences***

The vacation policy of the Commonwealth generally provides for the accumulation of 2.5 days per month, except for the teachers who accrue 4 days per month. Vacation time accumulated is fully vested to the employees from the first day of work up to a maximum of 60 days. Employees accumulate sick leave generally at a rate of 1.5 days per month up to a maximum of 90 days. Upon retirement, an employee receives compensation for all accumulated unpaid leave at the current rate, if the employee has at least 10 years of service with the Commonwealth. Accrued compensated absences of the primary government at June 30, 2003 amounting to approximately \$1.2 billion are presented in the statement of net assets. Compensated absence accumulation policies for the blended component units and component units vary from entity to entity based on negotiated agreements and other factors agreed upon between the management of these entities and their employees.

The Public Service Personnel Law requires certain component units and the primary government of the Commonwealth to annually pay the employees the accumulated vacation and sick leave earned in excess of the limits mentioned above.

**(w) *Interfund and Intraentity Transactions***

The Commonwealth has the following types of transactions among funds:

***Interfund Transfers*** – Legally required transfers that are reported when incurred as transfers-in by the recipient fund and as transfers-out by the disbursing fund, with receivables and payables presented as amounts due to and due from other funds. Advances between funds are also presented as amounts due to and due from other funds. However, these transfers and related amounts receivable and payable are considered internal balances and activities that have been eliminated in the government-wide financial statements.



## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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***Intraentity Transactions*** – There are two types of intraentity transactions. First are resource flows between the primary government and its component units and among the component units. These resource flows and related outstanding balances are reported as if they were external transactions. However, resource flows between the primary government and blended component units are classified as interfund transactions, as described above.

Second are intraentity balances between the primary government funds and discretely presented component units that are tantamount to long-term debt financing. The primary government's liability is reported in the statement of net assets, the proceeds in the primary government's funds, and the asset in the discretely presented component units' statement of net assets.

(x) ***Lottery Revenue and Prizes***

The revenue, expenses, and prizes awarded by the Lottery of Puerto Rico and the Additional Lottery System, reported within the lotteries enterprise fund, are recognized as drawings are held. Moneys collected prior to June 30 for tickets related to drawings to be conducted subsequent to June 30 are reported as deferred revenue. Unpaid prizes awarded as of June 30 are reported as a fund liability. For prizes payable in installments, the Commonwealth purchases deep discount securities through GDB, which are reported as restricted assets and lottery prizes payable.

(y) ***Risk Management***

The Commonwealth purchases commercial insurance covering casualty, theft, tort claims, and other losses for the primary government, most component units, and the municipalities. The Commonwealth is reimbursed for premium payments made on behalf of the component units and the municipalities. The current insurance policies have not been canceled or terminated. For workers' compensation, the Commonwealth has a discretely presented component unit, the SIFC, which provides workers' compensation to both, public and private employees. In the past three years, the Commonwealth has not settled claims that exceed insurance coverage.

Certain component units combine commercial insurance with internal self-insurance funds covering specific risks related to their specialized operations.

(z) ***Reclassifications***

Certain reclassifications have been made to the information presented in the separately issued financial statements of certain blended component units and agencies included within the special revenue, debt service, capital projects, and enterprise funds; and discretely presented component units to conform to the accounting classifications used by the Commonwealth in the basic financial statements.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

#### *(aa) Use of Estimates*

The preparation of the basic financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the basic financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

#### *(bb) Future Adoption of Accounting Pronouncements*

The GASB has issued the following accounting standards that have effective dates after June 30, 2003:

- GASB Statement No. 39, *Determining Whether Certain Organizations are Component Units*, which is effective for fiscal years beginning after June 15, 2003.
- GASB Statement No. 40, *Deposit and Investment Risk Disclosures an amendment of GASB Statement No. 3*, which is effective for fiscal years beginning after June 15, 2004.
- GASB Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries* which is effective for fiscal years beginning after December 15, 2004.
- GASB Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, which is effective for fiscal years beginning after December 15, 2004.
- GASB Statement No. 44, *Economic Condition Reporting: The Statistical Section—an amendment of NCGA Statement 1*, which is effective for statistical sections prepared for periods beginning after June 15, 2005.

The impact of these statements on the Commonwealth's basic financial statements has not yet been determined.

#### **(2) Component Units**

The Commonwealth follows the provisions of GASB No. 14. The basic financial statements of the Commonwealth include the financial statements of the following component units that were audited by other auditors:

Blended component units:

Public Buildings Authority  
Employees' Retirement System of the Government of Puerto Rico and its  
Instrumentalities  
Puerto Rico Judiciary Retirement System  
Puerto Rico System of Annuities and Pensions for Teachers

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

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### Discretely presented component units:

Agricultural Services and Development Administration  
Automobile Accident Compensation Administration  
Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico  
Employment and Training Enterprises Corporation  
Farm Insurance Corporation of Puerto Rico  
Fine Arts Center Corporation  
Governing Board of the 9-1-1 Service  
Land Authority of Puerto Rico  
Musical Arts Corporation  
National Parks Company of Puerto Rico  
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico  
Cooperatives  
Puerto Rico and Caribbean Cardiovascular Center Corporation  
Puerto Rico Aqueduct and Sewer Authority  
Puerto Rico Conservatory of Music Corporation  
Puerto Rico Convention Center District Authority  
Puerto Rico Council on Higher Education  
Puerto Rico Electric Power Authority  
Puerto Rico Exports Development Corporation  
Puerto Rico Health Insurance Administration  
Puerto Rico Highway and Transportation Authority  
Puerto Rico Land Administration  
Puerto Rico Maritime Transportation Authority  
Puerto Rico Medical Services Administration  
Puerto Rico Metropolitan Bus Authority  
Puerto Rico Ports Authority  
Puerto Rico Public Broadcasting Corporation  
Puerto Rico School of Plastic Arts  
Puerto Rico Solid Waste Authority  
Right to Employment Administration  
Special Communities Perpetual Trust  
State Insurance Fund Corporation  
University of Puerto Rico

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

#### (3) Stewardship, Compliance, and Accountability

##### (a) *Budgetary Control*

The Governor is constitutionally required to submit to the Legislature an annual balanced budget of the Commonwealth for the ensuing fiscal year. The annual budget is prepared by the Commonwealth's OMB and takes into consideration the advice provided by the Puerto Rico Planning Board (annual economic growth forecasts; four-year capital improvements plan), the Department of the Treasury of the Commonwealth (revenue estimates, accounting records, and the comprehensive annual financial report), GDB (fiscal agent), and other governmental offices and agencies. Section 7 of Article VI of the Constitution of Puerto Rico provides that "The appropriations made for any fiscal year shall not exceed the total revenue, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."

The annual budget, which is developed utilizing elements of performance-based program budgeting and zero-based budgeting, includes an estimate of revenue and other resources for the ensuing fiscal year under: (1) laws existing at the time the budget is submitted; and (2) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in her judgment are necessary, convenient, and in conformity with the four-year capital improvements plan adopted by the Puerto Rico Planning Board.

The Legislature may amend the budget submitted by the Governor but may not increase any items so as to cause a deficit without imposing taxes or identifying other sources of revenue to cover such deficit. Upon approval by the Legislature, the budget is referred to the Governor who may decrease or eliminate any line item but may not increase or insert any new line item in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature with her objections. The Legislature, by two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, the annual budget for the preceding fiscal year, as approved by the Legislature and the Governor, is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This permits the Commonwealth to continue making payments for its operating and other expenses until the new budget is approved. The appropriated annual budget for fiscal year 2003 amounted to approximately \$5 billion. The Legislature also made several special budgetary appropriations to the general fund throughout the year, which amounted to approximately \$2.8 billion.

The OMB has authority to amend the budget within a department, agency, or government unit without legislative approval.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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For budgetary purposes, encumbrance accounting is used. The encumbrances (that is, purchase orders, contracts) are considered expenditures when a commitment is made. For GAAP reporting purposes, encumbrances outstanding at year-end are reported as reservations of budgetary appropriations and GAAP fund balances and do not constitute expenditures or liabilities on a GAAP basis because the commitments will be honored during the subsequent year. The unencumbered balance of any appropriation of the general fund at the end of the fiscal year lapses immediately. Appropriations, other than in the general fund, are continuing accounts for which the Legislature has authorized that an unspent balance from the prior year be carried forward and made available for current spending.

In addition, the Legislature may direct that certain revenue be retained and made available for spending within a specific appropriation account. Generally, expenditures may not exceed the level of spending authorized for an individual department. However, the Commonwealth is statutorily required to pay debt service, regardless of whether such amounts are appropriated. Appropriations are enacted for certain departments, agencies, and government units included in the balance sheet of the general fund. For these funds, a statement of revenue and expenditures – budget and actual – budget basis – general fund is included. Appropriations for capital projects are made for each bond issue and the authorization continues for the expected construction period.

The Commonwealth's Department of the Treasury and OMB have the responsibility to ensure that budgetary spending control is maintained on an individual department basis. OMB may transfer part or all of any unencumbered balance within a department to another department subject to legislative approval. Budgetary control is exercised through the Puerto Rico Integrated Financial Accounting System (PRIFAS). PRIFAS ensures that encumbrances or expenditures are not processed if they exceed the department's total available spending authorization, which is considered its budget. The legal level of budgetary control is at the individual department level for general fund expenditures, principal and interest due for the year for the debt service fund, and by bond authorization for capital expenditures.

**(b) *Budget/GAAP Reconciliation***

The following schedule presents comparisons of the legally adopted budget with actual data on a budget basis. Because accounting principles applied for purposes of developing data on a budget basis differ significantly from those used to present financial statements in conformity with GAAP, a reconciliation of entity, timing, and basis differences in the excess (deficiency) of revenue and other

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

sources of financial resources over expenditures and other uses of financial resources for the year ended June 30, 2003 is presented below for the general fund (expressed in thousands):

Excess of expenditures and other financing uses over revenue and other sources – budget basis	\$ (13,962)
Entity differences:	
Excess (deficiency) of revenue and other sources over expenditures and other uses for:	
Nonbudgeted funds	(330,564)
Inclusion of agencies with independent treasuries	8,510
Timing differences:	
Adjustment for encumbrances	38,909
Current year expenditure against prior year encumbrances	(96,592)
Basis of accounting differences:	
Net increase in taxes receivable (net of tax refunds)	192,399
Net decrease in other receivables	(19,433)
Net increase in deferred revenue	(32,877)
Excess of expenditures and other financing uses over revenue and other financing sources (GAAP basis)	<u>\$ (253,610)</u>

**(c) Deficit Net Assets**

The following activities, funds, and discretely presented component units reflect deficit fund balance/net assets at June 30, 2003 (expressed in thousands):

Primary government:

Governmental activities	<u>\$ 11,952,784</u>
General fund	<u>\$ 140,296</u>
PBA capital projects fund	<u>\$ 80,183</u>
Enterprise fund – lotteries	<u>\$ 1,365</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### Component units:

Land Authority of Puerto Rico	\$ 148,194
Tourism Company of Puerto Rico	\$ 43,331
Puerto Rico and Caribbean Cardiovascular Center Corporation	\$ 32,021
Agricultural Services and Development Administration	\$ 35,561
Puerto Rico Medical Services Administration	\$ 11,359
Employment and Training Enterprises Corporation	\$ 6,686
Special Communities Perpetual Trust	\$ 5,356

The Commonwealth's governmental activities show a deficit of approximately \$12 billion, mostly attributed to long-term obligations amounting to approximately \$20 billion, which is recognized in the statement of net assets. On the other hand, the discretely presented component units report net assets of approximately \$16 billion. This inverse relationship between the governmental activities and component units' net assets reveal the operational structure of the Commonwealth where the primary government issues debt, the proceeds of which are predominantly transferred to the component units and to other governments as well, to finance their capital projects and other operational needs. The Commonwealth includes within the annual budgetary appropriation process the necessary funds to cover the annual debt service requirements of the aforementioned debt.

In the past, the Commonwealth has also provided financial resources to finance the deficit of component units. In addition, certain loans and obligations of TCPR and LAPR with GDB were restructured pursuant to Act No. 164, of December 17, 2001, described in note 14 (d).

### (4) Changes in Reporting Entity and Restatement

The following table illustrates the change to net assets at beginning of year as previously reported in the governmental activities' statement of net assets. The change resulted from inclusion in prior year of a capital asset that had been previously sold by a blended component unit (expressed in thousands):

Beginning net assets (deficit), as previously reported	\$ (10,171,632)
Restatement	<u>(34,065)</u>
Beginning net asset (deficit), as restated	<u>\$ (10,205,697)</u>

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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The following table illustrates the change to beginning fund balance as previously reported in the balance sheet by other governmental funds:

Beginning fund balance, as previously reported	\$ 887,985
PBA special revenue fund property reclassification from held for sale into held for use	(44,711)
The Children's Trust special revenue fund current year classification as a major fund	<u>(311,391)</u>
Beginning fund balance, as restated	\$ <u>531,883</u>

The following table summarizes changes to net assets at beginning of year as previously reported in the statement of net assets by certain discretely presented component units. The changes resulted primarily from exclusions of nonmajor component units in current years' presentation, and restatements to correct errors in the prior year's financial statements of certain nonmajor component units (expressed in thousands):

Beginning net assets, as previously reported	\$ 15,363,353
Nonmajor component units excluded in fiscal year 2003, but included in fiscal year 2002	(23,525)
Restatements of nonmajor component units	<u>(278)</u>
Beginning net assets, as restated	\$ <u>15,339,550</u>

#### (5) Puerto Rico Government Investment Trust Fund (PRGITF)

PRGITF was created by Act No. 176, of August 11, 1995, and began operations on December 4, 1995. PRGITF is a no-load diversified collective investment trust administered by GDB that was created for the purpose of providing eligible governmental investors of Puerto Rico with a convenient and economical way to invest in a professionally managed money market portfolio. PRGITF is not an investment company or a mutual fund and is not subject to regulation or registration under the investment company Act of 1940. Units issued by PRGITF are not subject to regulation or registration under the Securities and Exchange Act of 1933, as amended, because the units are issued by a government entity. The deposits on hand and the investments purchased are not collateralized, secured, or guaranteed by the Commonwealth or any of its agencies, instrumentalities, or political subdivisions.

PRGITF is considered a 2a7-like external investment pool, and as such, reports its investment at amortized cost.



# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

The investment securities on hand at June 30, 2003, consisted of certificates of deposit, bank notes, corporate obligations, commercial paper, and U.S. government and agencies obligations, all of which may be considered highly liquid. However, the participants' investments are subject to the ability of PRGIF to receive payment from the securities' issuer when due. The liquidity of certain investments and changes in interest rates may affect PRGIF's yield and the fair value of its investments.

The dollar amount of the deposits on hand at June 30, 2003, at \$1.00 per unit of participation, was reported in the individual financial statements of each of the participants, and combined in the basic financial statements as follows (expressed in thousands):

	<u>Balance outstanding</u>	<u>Percentage of total</u>
Primary government:		
Commonwealth	\$ 321,400	43.47%
The Children's Trust	272,710	36.88%
Office for the Improvement of the Public Schools	546	0.07%
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	<u>2</u>	<u>0.00%</u>
Total for primary government	<u>594,658</u>	<u>80.42%</u>
Discretely presented component units:		
Puerto Rico Land Administration	44,353	6.00%
State Insurance Fund Corporation	36,198	4.90%
Government Development Bank for Puerto Rico	23,511	3.20%
Tourism Company of Puerto Rico	12,941	1.75%
Puerto Rico Aqueduct and Sewer Authority	11,252	1.52%
Puerto Rico Solid Waste Authority	3,188	0.43%
Puerto Rico Infrastructure Financing Authority	1,764	0.24%
Puerto Rico Highway and Transportation Authority	300	0.04%
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico	226	0.04%
Puerto Rico School of Plastic Arts	142	0.03%
Puerto Rico Council of Higher Education	67	0.02%
Puerto Rico Electric Power Authority	<u>42</u>	<u>0.01%</u>
Total for discretely presented component units	<u>133,984</u>	<u>18.18%</u>
Other governmental entities	<u>10,725</u>	<u>1.40%</u>
Total for all participants	<u>\$ 739,367</u>	<u>100%</u>

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

The deposits at June 30, 2003 were invested in securities with a cost which approximates fair value, plus accrued interest, for approximately \$739 million. The external portion of PRGITF was not considered significant for separate reporting in the accompanying basic financial statements.

#### **(6) Deposits and Investments**

Under Commonwealth statutes, public funds deposited in commercial banks must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury's agents in the Commonwealth's name. In addition, the Commonwealth maintains deposits with GDB and EDB, two discretely presented component units, and the U.S. government (for unemployment insurance).

The Commonwealth's bank balance of deposits with financial institutions are categorized to provide an indication of the level of custodial credit risk assumed by the Commonwealth at year-end. Risk categories are described as follows:

**Category 1:** Insured or collateralized with securities held by the Secretary of the Treasury's agents in the Commonwealth's name.

**Category 2:** Collateralized with securities held by the pledging financial institution's trust department or agent in the Commonwealth's name.

**Category 3:** Uncollateralized (this includes any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the Commonwealth's name).

The Commonwealth's investments are categorized to provide an indication of the level of custodial credit risk assumed by the Commonwealth at year-end. Risk categories are described as follows:

**Category 1:** Insured or registered, or securities held by the Commonwealth or its agents in the Commonwealth's name.

**Category 2:** Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the Commonwealth's name.

**Category 3:** Uninsured and unregistered, with securities held by the counterparty or by its trust department or agent, but not in the Commonwealth's name.

Pursuant to the Statement of Investment Guidelines for the Government of Puerto Rico, the agencies and public corporations may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, bankers' acceptances, or in pools of obligations of the municipalities of Puerto Rico, among other things.

The public employees' retirement systems may invest in stocks, corporate bonds, U.S. mortgage loan obligations, private equity, and others.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

#### *Primary Government*

The carrying amount of deposits with financial institutions of the primary government at June 30, 2003 consists of the following (expressed in thousands):

Unrestricted:	
Carrying amount of deposits in commercial banks	\$ 90,582
Carrying amount of deposits in governmental banks	1,060,902
Carrying amount of deposits with the U.S. government	482,707
Subtotal	<u>1,634,191</u>
Restricted:	
Carrying amount of deposits in commercial banks	164,152
Carrying amount of deposits in governmental banks	1,031,161
Carrying amount of deposits with the U.S. government	48,563
Subtotal	<u>1,243,876</u>
Total carrying amount of deposits as reported on the primary government statement of net assets	<u>\$ 2,878,067</u>

Bank balance of deposits in commercial banks:

Category 1	\$ 184,444
Category 2	531,270
Category 3	72,604
Total bank balance of deposits in commercial banks	<u>\$ 788,318</u>

The bank balance of deposits in governmental banks, which as of June 30, 2003, is uninsured and uncollateralized, is approximately \$3.1 billion. These deposits are maintained with GDB and EDB. Deposits of approximately \$531 million with the U.S. government represent unemployment insurance taxes collected from employers that are transferred to the Federal Unemployment Insurance Trust Fund in the U.S. Treasury.

Unrestricted deposits include approximately \$321 million of deposits from the Commonwealth that are invested in PRGITF (see note 5). Such amount has been included as cash and cash equivalents in the primary government's statement of net assets.

Deposits in governmental banks represent the balance of interest and noninterest-bearing accounts in GDB and EDB. The deposit liability at GDB and EDB is substantially related to deposits from other component units and of the Commonwealth. The deposit liability does not agree with the governmental cash balances

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

shown because of reconciling items such as outstanding checks and deposits in transit. The bank balance of GDB's and EDB's deposits at June 30, 2003 is broken down as follows (expressed in thousands):

Primary government	\$ 1,852,893
Discretely presented components units	<u>1,244,594</u>
Total reporting entity	3,097,487
Municipalities of Puerto Rico	510,292
Other nongovernmental entities	226,429
Certificates of indebtedness	242,981
Escrow accounts	<u>171,056</u>
Total deposits per GDB and EDB	<u>\$ 4,248,245</u>

Custodial credit risk classification for short-term investments and investments of the primary government are as follows (expressed in thousands):

	Category			Carrying amount
	1	2	3	
Unrestricted:				
Mortgage notes	\$ 29	—	—	29
U.S. government and agencies securities	<u>35,995</u>	<u>—</u>	<u>—</u>	<u>35,995</u>
Subtotal	<u>36,024</u>	<u>—</u>	<u>—</u>	<u>36,024</u>
Investments not subject to categorization:				
Puerto Rico Government Investment Trust Fund				272,710
External investment pool				86,020
Guaranteed investment contracts				192,074
Other investments				<u>2,792</u>
Subtotal				<u>553,596</u>
Total – unrestricted				<u>589,620</u>
Restricted:				
Investments not subject to categorization – deep discount securities				<u>223,709</u>
Total – restricted				<u>223,709</u>
Total	<u>\$ 36,024</u>	<u>—</u>	<u>—</u>	<u>813,329</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Deep discount securities included as restricted investments are purchased through GDB to fund Lotto prizes of \$200,000 or more, payable on an installment basis. Investments in time deposits constitute collateral for the prizes. Annuity contracts are recorded at present value of future installment prize payments. Interest earned is not recognized as revenue, but credited to obligations for unpaid prize awards.

Local laws require that annuity contracts be held until maturity, unless the prizes to which they relate are not claimed within the statutory period. If not claimed, the annuities are canceled and proceeds thereof are transferred to the general fund.

### *Component Units*

Cash, cash equivalents, and investments of the component units at June 30, 2003 consist of (expressed in thousands):

	<u>Unrestricted</u>	<u>Restricted</u>	<u>Total</u>
Cash and cash equivalents	\$ 2,239,588	718,437	2,958,025
Investments	5,632,252	6,391,711	12,023,963
Total	<u>\$ 7,871,840</u>	<u>7,110,148</u>	<u>14,981,988</u>

Cash and cash equivalents consist of demand deposits, interest-bearing accounts, certificates of deposit, and bank investment contracts.

Information of carrying amounts and bank balances for deposits with financial institutions and bank investment contracts is as follows (expressed in thousands):

	<u>Carrying amount</u>	<u>Bank balance</u>
Deposits in commercial banks	\$ 2,419,012	2,407,788
Deposits in governmental banks	539,013	560,094
Total	<u>\$ 2,958,025</u>	<u>2,967,882</u>
Bank balances of deposits in banks:		
Category 1		\$ 2,384,460
Category 2		22,570
Category 3		560,852
Total bank balance of deposits in banks		<u>\$ 2,967,882</u>

The bank balance of deposits in governmental banks is uninsured and uncollateralized. Such deposits are maintained with GDB and EDB.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Custodial credit risk classification for short-term investments and investments of component units are as follows (expressed in thousands):

	Category			Carrying amount
	1	2	3	
Unrestricted:				
Mortgage-backed securities	\$ 259,692	—	9,999	269,691
U.S. government and agencies securities	2,393,142	8,311	153,788	2,555,241
Negotiable certificates of deposit	288,827	—	103,445	392,272
Stocks	447,127	—	15,317	462,444
Corporate bonds	377,755	—	21,514	399,269
Commercial paper	—	96,729	1,998	98,727
Repurchase agreements	64,712	—	4,914	69,626
Short-term investment	10,264	—	14,304	24,568
Foreign and municipal bonds	11,164	—	—	11,164
Money market funds	18,793	—	—	18,793
Other investments	340	—	—	340
Subtotal	<u>3,871,816</u>	<u>105,040</u>	<u>325,279</u>	<u>4,302,135</u>
Investments not subject to categorization:				
Guaranteed investment contracts				1,008,272
Puerto Rico Government Investment Trust Fund				115,850
Investment pool				148,896
Securities lending transactions underlying securities				49,954
Money market funds				4,145
Investment in equity securities				<u>3,000</u>
Total – unrestricted				<u>5,632,252</u>
Restricted:				
U.S. government and agencies securities	2,691,401	56,052	79,630	2,827,083
Foreign and municipal bonds	—	1,461,835	—	1,461,835
Mortgage-backed securities	—	889,752	—	889,752
Repurchase agreements	150,000	—	—	150,000
Negotiable certificates of deposit	2,981	—	17,551	20,532
Corporate bonds	12,154	1,912	—	14,066
Stocks	47,906	—	—	47,906
Subtotal	<u>\$ 2,904,442</u>	<u>2,409,551</u>	<u>97,181</u>	<u>5,411,174</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### Investments not subject to categorization:

Guaranteed investment contracts	\$	939,114
Investment pool		40,474
Puerto Rico Government Investment Trust Fund		442
Property held for sale		350
Money market funds/mutual funds		157
Total – restricted		<u>6,391,711</u>
Total	\$	<u>6,776,258</u> <u>2,514,591</u> <u>422,460</u> <u>12,023,963</u>

Unrestricted repurchase agreements of approximately \$64.7 million and \$4.9 million belong to EDB and SIFC, respectively. As of June 30, 2003, the fair value of the collateral for the repurchase agreements amounted to approximately \$67.2 million for EDB which consisted primarily of investment securities held in custody by EDB's agent, and \$4.9 million for SIFC, which consisted primarily of investment securities held by SIFC's agent but not in SIFC's name.

In addition, restricted repurchase agreements of approximately \$150 million belong to GDB. As of June 30, 2003, the fair value of the collateral for the repurchase agreements amounted to approximately \$150 million and consisted primarily of investment securities held in custody by GDB's agent.

Certain discretely presented component units classified approximately \$17.7 million of investments in PRGITF as cash and cash equivalents.

### *Fiduciary Funds*

The carrying amount of deposits with financial institutions of the fiduciary funds at June 30, 2003 consists of (expressed in thousands):

#### Unrestricted:

Carrying amount of deposits in commercial banks	\$	626,516
Carrying amount of deposits in governmental banks		<u>121,627</u>
Subtotal		<u>748,143</u>

#### Restricted:

Carrying amount of deposits in commercial banks		2,236
Carrying amount of deposits in governmental banks		<u>653</u>
Subtotal		<u>2,889</u>

Total carrying amount of deposits as reported on the statement of fiduciary net assets

\$ 751,032

Bank balance of deposits in commercial banks:

Category 1	\$	<u>628,752</u>
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# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

The bank balance of deposits in governmental banks, amounting to \$124.6 million at June 30, 2003, is uninsured and uncollateralized.

Custodial credit risk classification for short-term investments and investments of the fiduciary funds are as follows (expressed in thousands):

	Category			Carrying amount
	1	2	3	
Investment in preferred stock of PRTA Holdings	\$ —	—	362,670	362,670
Stocks	46	—	1,955,974	1,956,020
U.S. government and agencies securities	1,600	—	457,424	459,024
Mortgage bank securities	3,093	—	—	3,093
Corporate bonds	3,975	—	640,522	644,497
Short-term investments	3,185	—	—	3,185
State and local government bonds	1,196	—	—	1,196
Subtotal	13,095	—	3,416,590	3,429,685
Investments not subject to categorization:				
Mortgage loans				7
Limited partnerships/private equity				68,817
Total	\$ 13,095	—	3,416,590	3,498,509

Uninsured or unregistered investments at June 30, 2003 shown above belong mainly to the ERS.

ERS classified approximately \$2,000 of investments in PRGITF as cash and cash equivalents.

## (7) Securities Lending Transactions

### *Primary Government*

During the year, the ERS and the JRS, included within the fiduciary funds, SIFC and AACA, two discretely presented component units, entered into securities lending transactions. These transactions amounting to \$37.4 million, pertaining to the retirement systems, and \$131.4 million, pertaining to the discretely presented component units, at June 30, 2003, are included within investments and the corresponding securities lending liability in the statement of fiduciary net assets and the statement of net assets, respectively.



## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

#### **Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities and Puerto Rico Judiciary Retirement System (the Retirement Systems)**

The Retirement Systems' securities custodian, as agent for the Retirement Systems, manages the securities lending program and receives liquid collateral. The collateral requirement amounted to approximately \$38.4 million of the fair value of the securities lent. The collateral securities cannot be pledged or sold unless the borrower defaults. Securities lending obligations for which collateral was received as of June 30, 2003 consist of the following (expressed in thousands):

<u>Securities lent</u>	<u>Fair value of underlying securities</u>
Corporate bonds	\$ 9,557
U.S. government	13,479
Equity securities	<u>14,409</u>
	<u>\$ 37,445</u>

Collateral received amounted to \$38.4 million and it was invested as follows: \$5.1 million in commercial paper and \$27.3 million in repurchase agreements, \$3 million in promissory notes, and \$3 million in time and certificates of deposit. The relationship between the investment maturities and the Retirement Systems' loans cannot be determined.

At year-end, the Retirement Systems have no credit risk exposure to borrowers because the amounts the Retirement Systems owe the borrowers exceed the amounts the borrowers owe to the Retirement Systems. The Retirement Systems' rights to collateral are defined in the contractual agreements. The borrower's creditworthiness is also proactively reviewed by the lending agent.

#### ***Component Units***

##### **SIFC**

The Commonwealth statutes and the SIFC's board of directors' policies permit SIFC to use its investments to enter into securities lending transactions. The SIFC's securities custodian, as agent of SIFC, manages the securities lending program and receives cash, securities, or irrevocable bank letters of credit as collateral. The collateral securities cannot be pledged or sold by SIFC unless the borrower defaults. The collateral requirement is equal to 102% for securities issued in the United States and 105% for securities issued outside of the United States of the fair value of the securities lent. Additional collateral has to be provided by the next business day if its value falls to less than 100% of the fair value of the securities lent. At year-end, SIFC has no credit risk exposure to borrowers because the amounts SIFC owes the borrowers exceed the amounts the borrowers owe SIFC. Contracts with the lending agents require them to indemnify SIFC if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or fail to pay SIFC for income distributions by the securities' issuers while the securities are on loan.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

All security loans can be terminated on demand by either SIFC or the borrower, although the average term of the loans is two weeks. In lending securities, the term to maturity of the securities loans is matched with the term to maturity of the investment of the cash collateral. Such matching existed at year-end. Securities lending obligations for which cash was received as collateral as of June 30, 2003 consist of the following (expressed in thousands):

<b>Securities lent</b>	<b>Fair value of underlying securities</b>
Equity securities	\$ 15,317
U.S. government, agencies, and instrumentalities obligations	47,148
Corporate bonds and notes	14,487
	<u>\$ 76,952</u>

Cash collateral received amounted to \$77.9 million and it was invested as follows: \$4.9 million in repurchase agreements, \$7 million in corporate bonds and notes, \$54 million in interest-bearing deposits, \$2 million in commercial paper, and \$10 million in asset-backed securities.

In addition, SIFC had the following securities lending obligations collateralized by securities as of June 30, 2003 (expressed in thousands):

<b>Securities lent</b>	<b>Fair value of underlying securities</b>	<b>Securities collateral received</b>
U.S. government and agencies obligations	\$ 106,640	108,775

Securities lending transactions collateralized by securities that cannot be pledged or sold unless the borrower defaults are not reported as assets and liabilities in the accompanying balance sheets.

### AACA

AACA lends securities to broker/dealers and other entities (borrowers) for collateral that will be returned in the future for the same securities. The custodial bank manages the securities lending program and receives cash, government securities, and letters of credit as collateral. The program provides for an initial minimum collateralization of 102% of the market value of the securities lent plus accrued income. Additional collateral has to be provided by the close of the next business day if its value falls to less than 100%. The contract with the custodial bank requires that should a collateral deficiency occur beyond the custodian's responsibilities, the deficiency should be allocated pro rata among all client lenders within the program.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

Either the custodian bank or the borrower can terminate all security loans at any time. Cash collateral is invested in the program's agent short-term investment pools, which at fiscal year-end had a weighted average maturity of approximately 30 days. The relationship between securities of the investment pool and AACA loans cannot be determined.

The following represents the balances relating to the securities lending transactions as of June 30, 2003 (expressed in thousands):

<b>Securities lent</b>		<b>Fair value of underlying securities</b>	<b>Securities collateral received</b>
U.S. Treasury bills, bonds, and notes	\$	25,041	25,611
Common stocks and preferred stocks		12,108	12,456
Corporate bonds		7,531	7,721
U.S. agencies		9,733	9,981
Totals	\$	54,413	55,769

Securities lending transactions collateralized by securities that cannot be pledged or sold unless the borrower defaults do not have to be reported as assets and liabilities in the statement of net assets.

At year-end, AACA has no credit risk exposure to borrowers because the amounts AACA owes the borrowers exceed the amounts the borrowers owe AACA.

#### (8) Investments in Limited Partnerships

Pursuant to the Statement of Investment Guidelines for the Government of Puerto Rico, the pension trust funds and a component unit invested approximately \$8.7 million in limited partnerships during the fiscal year ended June 30, 2003. The investments were as follows:

- \$1.2 million were invested in Guayacán Funds of Funds, L.P., a Delaware limited partnership, organized by Grupo Guayacán, Inc. as general partner, that has total commitments of \$56 million of which \$45 million are from pension trust funds and the remaining balance from the private corporate investors. This fund invests in United States and international private equity partnerships that in turn invest in private companies.
- \$7.5 million were invested in Guayacán Fund of Funds II, L.P., a Delaware limited partnership, organized by Grupo Guayacán as general partner, that has total commitments of \$62 million of which \$50 million are from the pension trust funds and the remaining balance from the private corporate investors in Puerto Rico. The fund invests in a broad range of United States and international private equity investment partnerships that, in turn, will make equity and equity-related investments primarily in private businesses.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

- There were no contributions made during fiscal year 2003 in Guayacán Private Equity Fund, L.P., a Delaware limited partnership, organized by Advent/Morro Partners as general partner, that has total commitments of \$42 million of which \$10 million are from the pension trust funds, \$20 million are from a component unit and the remaining balance from the private corporate investors in Puerto Rico. This fund invests in Puerto Rico private equity.

The carrying value of these investments at June 30, 2003 amounted to \$65 million and is presented within investments in the statement of net assets. The allocations of net gain and net loss to the limited partners are based on certain percentages, as established in the limited partnership agreements.

As of June 30, 2003, the pension trust funds and a discretely presented component unit had capital commitments and contributions as follows (expressed in thousands):

<b>Guayacán Funds of Funds, L.P.</b>	<b><u>Public sector commitments</u></b>	<b><u>Fiscal year contributions</u></b>	<b><u>Cumulative contributions</u></b>
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	\$ 25,000	462	22,779
Puerto Rico System of Annuities and Pensions for Teachers	<u>20,000</u>	<u>770</u>	<u>18,623</u>
Subtotal	<u>45,000</u>	<u>1,232</u>	<u>41,402</u>
<b>Guayacán Fund of Funds II, L.P.</b>			
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	25,000	3,890	15,203
Puerto Rico System of Annuities and Pensions for Teachers	<u>25,000</u>	<u>3,641</u>	<u>14,954</u>
Subtotal	<u>50,000</u>	<u>7,531</u>	<u>30,157</u>
<b>Guayacán Private Equity Fund, L.P.</b>			
Primary government:			
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	5,000	—	3,930
Puerto Rico System of Annuities and Pensions for Teachers	<u>5,000</u>	<u>—</u>	<u>3,930</u>
Component unit – GDB	<u>20,000</u>	<u>—</u>	<u>15,718</u>
Subtotal	<u>30,000</u>	<u>—</u>	<u>23,578</u>
Total	<u>\$ 125,000</u>	<u>8,763</u>	<u>95,137</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### (9) Receivables and Payables

Receivables in the general fund include approximately \$1 billion of accrued income and excise taxes and \$296 million receivable from the federal government. In addition, the enterprise funds include \$63 million of accrued unemployment, disability, and drivers' insurance premium receivable.

Payables in the general fund include approximately \$1 billion of trade accounts due to suppliers for purchase of merchandise and services rendered and \$204 million of tax refunds liability.

### (10) Interfund and Intraentity Transactions

Interfund receivables and payables at June 30, 2003 are summarized as follows (expressed in thousands):

Due from/to other funds:

Receivable fund	Payable fund	Amount
Nonmajor governmental	PBA capital project funds	\$ 12,165
General fund	Enterprise fund – lotteries	28,602
General fund	Enterprise fund – unemployment insurance	16,698
Nonmajor governmental	General fund	70,869
PBA capital project fund	General fund	18,242
		<u>\$ 146,576</u>

Transfers from/to other funds:

Transferee fund	Transferor fund	Amount
Nonmajor governmental funds	General fund	\$ 252,823
Debt service fund	General fund	331,935
General fund	Nonmajor governmental funds	27,797
General fund	Enterprise fund – lotteries	219,311
Nonmajor enterprise funds	General fund	1,742
General fund	Enterprise fund – unemployment insurance	61,491
The Children's Trust – special revenue fund	Nonmajor governmental funds	61,388
General fund	The Children's Trust – special revenue fund	164,708
Nonmajor governmental funds	The Children's Trust – special revenue fund	544,825
		<u>\$ 1,666,020</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

The principal purposes of the interfund transfers are to:

- Distribute the increase in net assets of the lotteries fund for the use of the general fund, as required by the lotteries enabling legislation.
- Make funds available for debt service payments in both the debt service fund and the general fund.
- Unemployment insurance trust fund's distribution of surplus cash belonging to the general fund for the payment of administrative expenses.
- Recognize as transfers the rental payments made by the Commonwealth's agencies on properties leased by the nonmajor funds of the PBA, a blended component unit of the Commonwealth.

Interfund receivables and payables represent the pending settlements of the aforementioned transfers.

Due from/to primary government and component units are as follows (expressed in thousands):

<u>Receivable entity/fund</u>	<u>Amount</u>	<u>Payable entity/fund</u>	<u>Amount</u>
		Puerto Rico and Caribbean Cardiovascular Center Corporation	
Governmental activities	\$ 36,834		\$ 25,597
		Government Development Bank for Puerto Rico	
Business-type activities	138,428		6,924
		Governing Board of the 9-1-1 Service	
			4,313
		Puerto Rico Aqueduct and Sewer Authority	
			138,428
	<u>\$ 175,262</u>		<u>\$ 175,262</u>
<u>Receivable entity/fund</u>	<u>Amount</u>	<u>Payable entity/fund</u>	<u>Amount</u>
Puerto Rico Electric Power Authority	\$ 42,069	Governmental activities	\$ 142,513
University of Puerto Rico	56,040		
Puerto Rico Metropolitan Bus Authority	1,164		
Government Development Bank for Puerto Rico	26,268		
Puerto Rico Infrastructure Financing Authority	1,200		
Agricultural Services and Development Administration	13,126		
Puerto Rico Maritime Transportation Authority	2,646		
	<u>\$ 142,513</u>		<u>\$ 142,513</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

The amount owed by PRASA of \$138 million represents construction loans granted by the Puerto Rico Water Pollution Control Revolving Fund, a nonmajor enterprise fund, to finance the construction of capital assets for PRASA.

The amount receivable by PREPA from the primary government includes \$32 million representing an agreement with the Commonwealth by which the Commonwealth will pay the outstanding fuel adjustment subsidy receivable which amounted originally to \$94 million. This amount owed by the Commonwealth is presented within notes payable in the statement of net assets of the governmental activities.

The amount receivable by the UPR from primary government includes a resolution approved by the Legislature to pay \$48.4 million to the UPR on behalf of the Department of Health of the Commonwealth over eight years. The related outstanding balance of \$31 million is presented by the Commonwealth within notes payable in the statement of net assets of the governmental activities.

Due to from/to component units are as follows (expressed in thousands):

<u>Receivable entity</u>	<u>Amount</u>	<u>Payable entity</u>	<u>Amount</u>
Tourism Company of Puerto Rico	\$ 100,821	Puerto Rico Convention Center District Authority	\$ 100,821
University of Puerto Rico	11,426	Puerto Rico Medical Services Administration	11,426
Economic Development Bank for Puerto Rico	9,611	Puerto Rico Exports Development Corporation	9,611
Puerto Rico Electric Power Authority	11,688	Puerto Rico Medical Services Administration	11,688
Puerto Rico Ports Authority	15,128	Puerto Rico Maritime Transportation Authority	15,128
Farm Insurance Corporation of Puerto Rico	7,470	Agricultural Services and Development Administration	7,470
Puerto Rico Aqueduct and Sewer Authority	22,196	Puerto Rico Infrastructure Financing Authority	22,196
Land Authority of Puerto Rico	17,367	Agricultural Services and Development Administration	17,367
Puerto Rico Infrastructure Financing Authority	18,000	Puerto Rico Aqueduct and Sewer Authority	18,000
Balance carried forward	\$ <u>213,707</u>		\$ <u>213,707</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Balance brought forward	\$	213,707		\$	213,707
Government Development Bank for Puerto Rico		764,877	Puerto Rico Aqueduct and Sewer Authority		38,161
			Puerto Rico Infrastructure Financing Authority		9,800
			University of Puerto Rico		17,508
			Puerto Rico Electric and Power Authority		60,000
			Economic Development Bank for Puerto Rico		13,095
			Puerto Rico Ports Authority		250,493
			Puerto Rico Industrial Development Company		78,722
			Tourism Company of Puerto Rico		105,392
			Agricultural Services and Development Administration		20,498
			Land Authority of Puerto Rico		72,595
			Puerto Rico Metropolitan Bus Authority		5,428
			Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority		128,302
			Puerto Rico Solid Waste Authority		7,608
			Employment and Training Enterprises Corporation		2,135
			Special Communities Perpetual Trust		4,952
					<u>814,689</u>
	\$	<u>978,584</u>		\$	<u>1,028,396</u>



## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

The difference between due from/to component units resulted predominantly from the existence of \$43.9 million debt payable by the Land Authority to GDB, classified as an off-balance sheet by GDB as this debt represents past nonaccruing interest on a related loan.

The balances due to GDB amounting to \$814.7 million represent loan payable to GDB at June 30, 2003.

The rest of the loans receivable reported by GDB consists of the following (expressed in thousands):

Primary government:	
Governmental activities	\$ 701,745
Business-type activities	<u>1,308</u>
	703,053
Other governmental entities and municipalities	857,686
Private sector (net of \$35,071 presented within restricted assets)	<u>275,577</u>
Total loans receivable	\$ <u><u>1,836,316</u></u>

The loans to the primary government are presented by the Commonwealth within notes payable in the statement of net assets. A difference of \$141,000 resulted from the time lag between the dates that transactions are recorded by GDB and the primary government.

Expenses of the primary government include approximately \$2.7 billion in capital and operational contributions to the component units, comprised as follows (expressed in thousands):

Puerto Rico Health Insurance Administration	\$ 963,439
University of Puerto Rico	696,242
Puerto Rico Aqueduct and Sewer Authority	443,847
Puerto Rico Infrastructure Financing Authority	74,732
Nonmajor component units	<u>482,425</u>
Total contributions made by primary government to component units	\$ <u><u>2,660,685</u></u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### (11) Restricted Assets

Restricted assets of the primary government included in the basic financial statements at June 30, 2003 consist of cash, investments, and other assets to be used for the following purposes (expressed in thousands):

Primary government:		
Debt service and sinking fund requirements	\$	910,458
Payment of lottery prizes		223,709
Emergency fund		100,000
Construction fund		57,943
QZAB		50,191
Cash available for deposit to sinking fund		19,224
Other restricted assets of the Public Housing Administration		31,354
Administrative costs for unemployment insurance		48,563
Residual receipts from sale of properties		21,329
Proceeds from sales of assets		4,089
Restricted for the payment of salaries under Act No. 82		<u>725</u>
Total for primary government	\$	<u>1,467,585</u>

Liabilities of the primary government payable from restricted assets consist of the following (expressed in thousands):

Governmental activities:		
Accounts payable	\$	90,877
Interest payable		17,188
Tax revenue anticipation notes payable		800,000
Deferred revenue		<u>94,297</u>
Liabilities payable from restricted assets – governmental activities	\$	<u>1,002,362</u>
Business-type activities:		
Lottery prizes payable within one year	\$	6,404
Lottery prizes payable after one year		<u>217,305</u>
Liabilities payable from restricted assets – business-type activities	\$	<u>223,709</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Restricted assets of the component units included in the basic financial statements at June 30, 2003 are to be used for the following purposes (expressed in thousands):

Component units:

Debt service and sinking fund requirements	\$	3,691,596
Construction and betterments funds		2,405,982
Escrow		95,114
Contingency reserve		8,556
Self-insurance fund		80,245
Maintenance reserve fund		48,276
Educational fund		72,482
Development of infrastructure projects		23,249
Payment of incentives to farmers		10,102
Malpractice insurance fund		1,500
Reserve for reinsurance claims		2,125
General reserve fund		1,474
Severance payment		3,000
Film industry development activities		6,816
Purchase of assets		1,469
Renewal and replacement fund		2,273
Judicial claim fund		863
Financial assistance programs		559,243
EPA monitoring		160
Other		130,694
Total for components units	\$	<u>7,145,219</u>

## (12) Capital Assets

Capital assets activity for the year ended June 30, 2003 is as follows (expressed in thousands):

### Primary Government

	<u>Beginning balance (as restated)</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending balance</u>
Governmental activities:				
Capital assets, not being depreciated:				
Land	\$ 1,097,793	31,559	235,032	894,320
Construction in progress	1,108,402	497,357	641,151	964,608
Total capital assets, not being depreciated	\$ <u>2,206,195</u>	<u>528,916</u>	<u>876,183</u>	<u>1,858,928</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

	<b>Beginning balance (as restated)</b>	<b>Increases</b>	<b>Decreases</b>	<b>Ending balance</b>
Capital assets, being depreciated:				
Buildings and building improvements	\$ 4,673,013	989,820	45,928	5,616,905
Equipment	263,966	71,958	11,713	324,211
Total capital assets, being depreciated	<u>4,936,979</u>	<u>1,061,778</u>	<u>57,641</u>	<u>5,941,116</u>
Less accumulated depreciation for:				
Buildings and building improvements	1,602,041	234,239	40,236	1,796,044
Equipment	137,308	35,587	9,984	162,911
Total accumulated depreciation	<u>1,739,349</u>	<u>269,826</u>	<u>50,220</u>	<u>1,958,955</u>
Total capital assets, being depreciated, net	<u>3,197,630</u>	<u>791,952</u>	<u>7,421</u>	<u>3,982,161</u>
Governmental activities capital assets, net	<u>\$ 5,403,825</u>	<u>1,320,868</u>	<u>883,604</u>	<u>5,841,089</u>
Business-type activities:				
Total capital assets, being depreciated – equipment	\$ 4,754	65	—	4,819
Less accumulated depreciation of equipment	<u>2,559</u>	<u>365</u>	<u>—</u>	<u>2,924</u>
Total business-type activities capital assets, being depreciated, net	<u>\$ 2,195</u>	<u>(300)</u>	<u>—</u>	<u>1,895</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Depreciation expense was charged to functions/programs of the primary government for the year ended June 30, 2003 as follows (expressed in thousands):

Governmental activities:	
General government	\$ 45,523
Public safety	93,623
Health	3,903
Public housing and welfare	87,658
Education	25,030
Economic development	14,089
Total depreciation expense – governmental activities	\$ 269,826
Total depreciation business-type activities – lotteries	\$ 365

The capital assets of the primary government were changed (increased) as of the beginning of the year by approximately \$10 million to reflect certain correcting and reclassifications activities recognized by Public Housing Administration and Public Building Authority. The Public Housing Administration, a Commonwealth agency forming part of the general fund, restated (decreased) capital assets in the amount of \$34 million to correct sale of capital assets not previously reflected. PBA increased capital assets in the amount of \$44 million to reflect a change in intention in the use of certain assets from held for sale to held for use (see note 4).

On August 17, 2001, the Legislature of the Commonwealth approved Act 120, which requires the conditional transfer of the ownership of certain real properties under the name of the Department of Recreation and Sports (DRS) of the Commonwealth to the municipalities of Commonwealth. The property consisted of certain recreational and sport facilities located throughout Puerto Rico. The land and the facilities were transferred at no cost to the municipalities. During fiscal year ended June 30, 2003, land, buildings, and building improvements with a cost of approximately \$204 million were transferred to several municipalities and recorded as a special item in the accompanying statement of activities for the year ended June 30, 2003 to give effect to these transactions.

### *Discretely Presented Component Units*

	Beginning balance (as restated)	Increases	Decreases	Ending balance
Capital assets, not being depreciated:				
Land	\$ 2,244,391	120,111	6,123	2,358,379
Art works	3,081	650	1,646	2,085
Construction in progress	7,500,121	1,453,001	220,183	8,732,939
Total capital assets, not being depreciated	\$ 9,747,593	1,573,762	227,952	11,093,403

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

	<b>Beginning balance (as restated)</b>	<b>Increases</b>	<b>Decreases</b>	<b>Ending balance</b>
Capital assets, being depreciated:				
Buildings and building improvements	\$ 7,377,968	131,309	18,848	7,490,429
Equipment	1,972,621	225,948	49,869	2,148,700
Infrastructure	16,513,605	181,128	17,896	16,676,837
Total capital assets, being depreciated, carried forward	25,864,194	538,385	86,613	26,315,966
Less accumulated depreciation for:				
Buildings and building improvements	3,955,210	286,895	32,225	4,209,880
Equipment	505,955	82,072	19,405	568,622
Infrastructure	6,917,016	365,790	10,910	7,271,896
Total accumulated depreciation	\$ 11,378,181	734,757	62,540	12,050,398
Total capital assets, being depreciated, net	\$ 14,486,013	(196,372)	24,073	14,265,568
Capital assets, net	\$ 24,233,606	1,377,390	252,025	25,358,971

The capital assets of the discretely presented component units were changed as of the beginning of the year primarily as a result of the exclusion of component units in the current year (see note 4).

### (13) Tax Revenue Anticipation Notes Payable

Tax revenue anticipation notes (TRANS) reported in the general fund, were issued on October 3, 2002, at an interest rate of 2.50% and were paid on July 30, 2003. The TRANS amounted to \$800 million at June 30, 2003 plus accrued interest of approximately \$14.8 million. The proceeds of the TRANS were used to cover a temporary cash deficiency resulting from the timing differences between tax collections and the payments of current expenditures.

### (14) Long-Term Obligations

#### *Primary Government*

#### *(a) Summary of Short and Long-Term Obligations*

Long-term obligations at June 30, 2003 and changes for the fiscal year then ended are as follows (expressed in thousands):

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

	Balance at June 30, 2002	Debt/ refunding debt issued	Capitalized interest	Debt paid or defeased	Notes payable refunded	Net original issue (discounts) premiums	Discount accretion	Other net increases (decreases)	Balance at June 30, 2003	Due within one year
<b>Governmental activities:</b>										
Bonds payable	\$ 8,701,289	3,300,873	29,575	(2,282,615)	—	139,877	1,968	(235,615)	9,655,352	147,660
Commonwealth appropriation bonds	2,839,905	—	—	(42,543)	—	—	69	—	2,797,431	58,564
Notes payable:										
Third parties	1,027,661	—	17,157	(3,517)	—	—	—	—	1,041,301	1,031,662
Component units:										
GDB	271,961	2,253,001	—	(1,812,027)	(11,331)	—	—	—	701,604	187,671
Other	70,207	—	—	(7,570)	—	—	—	—	62,637	20,224
Compensated absences	1,193,796	—	—	(879,906)	—	—	—	836,551	1,150,441	847,370
Net pension obligation	3,220,050	—	—	—	—	—	—	581,763	3,801,813	—
Obligation under capital leases	115,433	58,897	—	(11,359)	—	—	—	—	162,971	11,081
Other liabilities:										
Employees' Christmas bonus	77,160	—	—	(132,275)	—	—	—	156,738	101,623	101,623
Liability for federal cost	41,443	—	—	—	—	—	—	10,646	52,089	52,089
Liability for legal claims and judgments	78,228	—	—	(30,144)	—	—	—	20,618	68,702	64,722
Other	2,500	—	—	—	—	—	—	82	2,582	—
<b>Total governmental activities</b>	<b>17,639,633</b>	<b>5,612,771</b>	<b>46,732</b>	<b>(5,201,956)</b>	<b>(11,331)</b>	<b>139,877</b>	<b>2,037</b>	<b>1,370,783</b>	<b>19,598,546</b>	<b>2,522,666</b>
<b>Business-type activities:</b>										
Debts payable to component units	1,053	255	—	—	—	—	—	—	1,308	700
Notes payable to third parties	1,885	—	—	(808)	—	—	—	—	1,077	74
Compensated absences	3,936	—	—	(2,970)	—	—	—	2,743	3,709	2,388
Obligation for unpaid lottery prizes	297,167	—	—	(409,228)	—	—	—	386,837	274,776	57,471
Liability for insurance benefits, including IBNR	150,088	—	—	(318,790)	—	—	—	348,771	180,069	180,069
Other long-term liabilities:										
Employees' Christmas bonus	254	—	—	(435)	—	—	—	532	351	351
<b>Total business-type activities</b>	<b>454,383</b>	<b>255</b>	<b>—</b>	<b>(732,231)</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>738,883</b>	<b>461,290</b>	<b>241,053</b>
<b>Total governmental and business-type</b>	<b>\$ 18,094,016</b>	<b>5,613,026</b>	<b>46,732</b>	<b>(5,934,187)</b>	<b>(11,331)</b>	<b>139,877</b>	<b>2,037</b>	<b>2,109,666</b>	<b>20,059,836</b>	<b>2,763,719</b>

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

The other net increases in bonds and notes payable consist of deferred losses on refunding, net of amortization, and amortization of premiums on bonds. These adjustments did not require any source or use of cash.

Compensated absences, net pension obligation, obligation for unpaid lottery awards, liability for insurance benefits, and other long-term liabilities reflect other net increases (decreases) resulting from adjustments and changes to agree these obligations to their estimated balances at June 30, 2003.

#### **(b) Debt Limitation**

The Constitution of the Commonwealth authorizes the contracting of debts as determined by the Legislature. Nevertheless, the Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by bonds or notes and backed by the full faith, credit, and taxing power of the Commonwealth, are not to be issued if the amount of the principal of, and interest on, such bonds and notes and on all such bonds and notes issued thereafter which are payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenue raised under the provisions of Commonwealth legislation and conveyed into the Treasury (hereinafter internal revenue) in the two fiscal years preceding the then current fiscal year. Section 2, Article VI of the Constitution does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded. Internal revenue consists principally of income taxes and excise taxes. Certain revenue, such as federal excise taxes on offshore shipments of alcoholic beverages, tobacco products, and customs duties, which are collected by the U.S. government and returned to the Commonwealth, and motor vehicle fuel taxes and license fees, which are allocated to the PRHTA, a discrete component unit, are not included as revenue for the purpose of calculating the debt limit, although they may be available for the payment of debt service. At June 30, 2003, the Commonwealth is in compliance with the debt limitation requirement.

#### **(c) Bonds Payable**

The Constitution of the Commonwealth provides that public debt will constitute a first claim on the available revenue of the Commonwealth. Public debt includes general obligations and notes of the Commonwealth and any payment required to be made by the Commonwealth under its guarantees of bonds issued by blended or discretely presented component units. The good faith, credit, and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal and interest of the general obligation bonds.

Act No. 83 of August 30, 1991, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation. The levy is made by the CRIM, a municipal corporation, not a component unit of the Commonwealth. CRIM is required to remit the 1.03% of property tax collected to the Commonwealth to be used by the



# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Commonwealth's debt service fund for payment of debt service on general obligations of the Commonwealth. During the year ended June 30, 2003, the total revenue and receivable reported by the Commonwealth amounted to approximately \$113 million and \$30 million, respectively, which are included in the debt service fund.

For financial reporting purposes, the outstanding amount of bonds represents the total principal to be repaid, net of unamortized premiums, discount and deferred refunding losses; for capital appreciation bonds, it represents total principal and accreted interest to be repaid.

Bonds payable outstanding at June 30, 2003 is as follows (expressed in thousands):

	<u>General obligation</u>	<u>Revenue bonds</u>	<u>Total</u>
Term bonds payable through 2036; interest payable semiannually at rates varying from 3% to 8%.	\$ 2,643,980	816,125	3,460,105
Serial bonds payable through 2024; interest payable semiannually at rates varying from 3.75% to 7.5%.	3,275,455	1,055,535	4,330,990
Capital appreciation bonds payable through 2031; no interest rate, yield ranging from 4.42% to 7.8%. Net of accreted discount of \$190 million.	251,345	184,720	436,065
The Children's Trust fund tobacco settlement asset-backed bonds payable through 2026; interest payable annually at rates varying from 4.625% to 6%.	—	1,157,240	1,157,240
New housing authority bonds payable through 2010; interest payable annually at rates ranging from 2.125% to 6%.	—	81,580	81,580
Appropriation refunding bonds for low-income housing payable through 2005; interest payable at rates varying from 6.9% to 8%.	34,775	—	34,775
Bond payment obligation payable through 2008; interest payable at rates varying from 3.5% to 5.5%.	33,450	—	33,450
Balance carried forward	\$ 6,239,005	3,295,200	9,534,205

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

	<u>General obligation</u>	<u>Revenue bonds</u>	<u>Total</u>
Balance brought forward	\$ 6,239,005	3,295,200	9,534,205
Bond payment obligation payable through 2009; interest payable at rates varying from 3.5% to 5.5%.	44,240	—	44,240
Bond payment obligation payable through 2010; interest payable at rates varying from 1.5% to 5.5%.	48,220	—	48,220
Yield curve bonds payable from 2009 through 2011; no interest rate, yield of 8.914%.	15,000	—	15,000
Tax-exempt components maturing through 2007 and 2008; interest at rates ranging from 5.5% to 5.6%.	—	72,160	72,160
Inverse rate bonds payable from 2009 through 2011, at an interest rate of 6%.	15,000	—	15,000
Total	6,361,465	3,367,360	9,728,825
Unamortized premium (discount)	228,176	(28,003)	200,173
Deferred charges arising from debt refunding	(183,210)	(90,667)	(273,877)
Savings bonds	231	—	231
Total bonds payable	<u>\$ 6,406,662</u>	<u>3,248,690</u>	<u>9,655,352</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

During the year ended June 30, 2003, the following changes occurred in the bonds payable (expressed in thousands):

	<b>Outstanding June 30, 2002</b>	<b>Issued</b>	<b>Premiums/ discount (redemptions)</b>	<b>Outstanding June 30, 2003</b>
Term bonds	\$ 3,524,225	1,295,690	(1,359,810)	3,460,105
Serial bonds	3,838,295	773,825	(281,130)	4,330,990
Capital appreciation bonds	457,574	60,158	(81,667)	436,065
The Children's Trust tobacco settlement asset-backed bonds	390,170	1,171,200	(404,130)	1,157,240
New housing authority bonds	92,740	—	(11,160)	81,580
Appropriation refunding bonds	57,630	—	(22,855)	34,775
Bond payment obligations	125,910	—	—	125,910
Yield curve bonds	15,000	—	—	15,000
Tax-exempt components	72,160	—	—	72,160
Deferred interest bonds	50,000	—	(50,000)	—
Indexed inverse floaters	46,000	—	(46,000)	—
Inverse rate bonds	15,000	—	—	15,000
Subtotal	8,684,704	3,300,873	(2,256,752)	9,728,825
Unamortized premium	68,327	—	131,846	200,173
Deferred charges arising from debt refunding	(51,973)	—	(221,904)	(273,877)
Savings bonds	231	—	—	231
Total	<u>\$ 8,701,289</u>	<u>3,300,873</u>	<u>(2,346,810)</u>	<u>9,655,352</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Maturities of general obligations and of revenue bonds payable, including accrued interest of capital appreciation bonds are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 147,660	473,129	620,789
2005	160,375	471,804	632,179
2006	243,560	473,603	717,163
2007	215,784	488,875	704,659
2008	238,394	481,756	720,150
2009-2013	1,652,065	1,986,819	3,638,884
2014-2018	1,937,129	1,609,465	3,546,594
2019-2023	1,792,306	1,058,634	2,850,940
2024-2028	1,292,090	657,864	1,949,954
2029-2033	1,152,429	402,068	1,554,497
2034-2038	439,070	164,092	603,162
2039-2043	334,844	63,132	397,976
Total	9,605,706	<u>8,331,241</u>	<u>17,936,947</u>
Plus accreted discount	123,350		
Plus: unamortized premium	200,173		
Less: deferred charges arising from debt refunding	<u>(273,877)</u>		
Total	\$ <u>9,655,352</u>		

### (d) *Commonwealth Appropriation Bonds*

Over the years, GDB, as fiscal agent and bank for the Commonwealth, had extended lines of credit, advances, and loans to several agencies and blended component units in order to finance their capital improvement projects and to cover their operational deficits at the time. At different points in time, these loans were refunded through the issuance of Commonwealth appropriation bonds issued by the Puerto Rico Public Finance Corporation (PFC), a blended component unit of GDB. PFC is the financing arm of GDB which serves only as conduit for the issuance of the bonds. The repayment source for these bonds consists of Commonwealth appropriations submitted for approval of the Legislature annually during the budget preparation process of the Commonwealth. The Legislature is not legally bound to appropriate funds for such repayments.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

The outstanding balance of the Commonwealth appropriation bonds is comprised of the following refunded obligations (expressed in thousands):

Health Facilities and Services Administration	\$	547,908
Office for the Improvement of Public Schools		348,060
Puerto Rico Maritime Shipping Authority		270,145
Property tax settlement		129,144
Act No. 164 restructuring:		
PFC 2002 Series A		578,276
PFC 2002 Series B		12,018
PFC 2001 Series C		344,618
PFC 2001 Series D		40,750
PFC 2001 Series E		526,512
Total Commonwealth appropriation bonds	\$	<u>2,797,431</u>

As of July 1, 1999, approximately \$595 million (including unpaid interest) of a promissory note of the Health Facilities and Services Administration (HFSA) due to GDB was transferred to the Department of Health of the Commonwealth and restructured through Commonwealth appropriation bonds. The bonds bear interest at rates ranging between 5.90% and 6.20%. Principal and interest on the bonds are payable solely from legislative appropriations to be made pursuant to Act No. 223 of August 9, 1998. The act provides that OMB shall include in the annual budget of the Commonwealth an amount equal to \$56.5 million for the fiscal year 1998-99, and for the next succeeding 15 fiscal years the amount necessary to pay the principal of and interest on the bonds, up to a maximum annual amount of \$57.7 million. As of June 30, 2003, approximately \$548 million were still outstanding.

Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 22,082	32,875	54,957
2005	26,150	31,550	57,700
2006	27,719	29,981	57,700
2007	29,383	28,317	57,700
2008	31,146	26,554	57,700
2009-2013	186,105	102,395	288,500
2014-2018	225,323	13,519	238,842
Total	\$ <u>547,908</u>	<u>265,191</u>	<u>813,099</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Previous public schools infrastructure improvement loans provided additional funds for major repairs and improvements to the public schools in Puerto Rico. This activity is administered by the Office for the Improvement of the Public Schools of Puerto Rico (OIPS), included as part of the general fund of the primary government. These loans were refunded through the issuance of Commonwealth appropriation bonds pursuant to Act No. 85 of June 13, 1998 (Act 85). The bonds bear interest at rates ranging from 5.0% to 5.85%. As of June 30, 2003, approximately \$348 million were outstanding. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 8,290	17,925	26,215
2005	8,725	17,488	26,213
2006	9,090	17,128	26,218
2007	9,470	16,746	26,216
2008	9,945	16,273	26,218
2009-2013	58,090	72,988	131,078
2014-2018	75,425	55,654	131,079
2019-2023	97,640	33,438	131,078
2024-2026	71,385	7,269	78,654
Total	<u>\$ 348,060</u>	<u>254,909</u>	<u>602,969</u>

A promissory note payable owed by PRMSA to GDB was assumed by the Commonwealth in connection with the sale of the maritime operations of PRMSA. Commonwealth appropriation bonds were issued to refund this liability. The bonds bear interest at a variable rate ranging from 3.00% to 7.30%. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 7,235	16,941	24,176
2005	7,730	16,426	24,156
2006	8,265	15,889	24,154
2007	8,850	15,304	24,154
2008	9,455	14,697	24,152
2009-2013	58,210	62,384	120,594
2014-2018	57,464	62,993	120,457
2019-2023	62,027	58,005	120,032
2024-2026	39,548	22,227	61,775
Total	<u>258,784</u>	<u>284,866</u>	<u>543,650</u>
Plus accreted discount	<u>11,361</u>		
Total	<u>\$ 270,145</u>		

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

During fiscal year 1996, the Commonwealth refinanced the liability for the settlement of the property taxes owed to the municipalities of Puerto Rico. Commonwealth appropriation bonds were issued to refund this liability. The bonds were issued for approximately \$192 million, bearing interest at rates ranging from 5.87% to 7.25%. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 11,185	6,755	17,940
2005	12,415	5,991	18,406
2006	13,310	5,083	18,393
2007	14,285	4,103	18,388
2008	15,350	3,040	18,390
2009-2013	52,477	39,487	91,964
2014-2017	10,122	26,678	36,800
Total	<u>\$ 129,144</u>	<u>91,137</u>	<u>220,281</u>

On December 17, 2001, Act No. 164 was approved, which authorized certain government agencies and discretely presented component units to refund approximately \$2.4 billion of their outstanding obligations with GDB, for which no repayment source existed, over a period not exceeding 30 years, and to be repaid with annual Commonwealth appropriations not to exceed \$225 million. This refunding was done with Commonwealth appropriation bonds through several series issued by PFC during the period between December 2001 and June 2002.

Approximately \$1.5 billion of the aforementioned outstanding obligations belonged to the primary government, predominantly the Department of Health of the Commonwealth (health reform financing and other costs for approximately \$1.1 billion) and the Department of the Treasury of the Commonwealth (the fiscal year 2001 deficit financing of \$268 million and the obligation assumed for defective tax liens in the amount of approximately \$132 million). These obligations were refunded under the following series of Commonwealth appropriation bonds:

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

**PFC 2002 Series A** – This series bearing interest rates from 5.45% to 6.25% has the following debt service requirements (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ —	33,314	33,314
2005	—	33,314	33,314
2006	—	33,314	33,314
2007	—	33,314	33,314
2008	17,386	32,446	49,832
2009-2013	119,235	156,252	275,487
2014-2018	161,862	129,112	290,974
2019-2023	212,979	69,684	282,663
2024-2025	102,945	3,768	106,713
	614,407	524,518	1,138,925
Discount, net	(36,131)		
Total	\$ <u>578,276</u>		

**PFC 2002 Series B** – This series bearing interest rates from 4.95% to 5.05% has the following debt service requirements (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ —	603	603
2005	—	603	603
2006	—	603	603
2007	—	603	603
2008	4,327	406	4,733
2009	7,691	32	7,723
Total	\$ <u>12,018</u>	<u>2,850</u>	<u>14,868</u>



# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

**PFC 2001 Series C** – This series bearing interest rates from 4% to 6.15% has the following debt service requirements (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 8,522	19,876	28,398
2005	8,606	19,493	28,099
2006	2,149	19,367	21,516
2007	1,553	19,287	20,840
2008	11,081	18,732	29,813
2009-2013	66,205	83,859	150,064
2014-2018	87,840	65,915	153,755
2019-2023	118,976	30,093	149,069
2024-2025	45,371	1,261	46,632
	<u>350,303</u>	<u>277,883</u>	<u>628,186</u>
Discount, net	<u>(5,685)</u>		
Total	\$ <u>344,618</u>		

**PFC 2001 Series D** – This series bearing interest rates from 3.7% to 5% has the following debt service requirements (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 1,250	1,921	3,171
2005	2,000	1,838	3,838
2006	17,500	1,069	18,569
2007	20,000	83	20,083
Total	\$ <u>40,750</u>	<u>4,911</u>	<u>45,661</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

**PFC 2001 Series E** – This series bearing interest rates from 5.5% to 6% has the following debt service requirements (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ —	29,873	29,873
2005	—	29,873	29,873
2006	—	29,873	29,873
2007	—	29,873	29,873
2008	—	29,873	29,873
2009-2013	—	149,363	149,363
2014-2018	—	149,363	149,363
2019-2023	—	149,363	149,363
2024-2028	229,153	131,405	360,558
2029-2031	299,506	25,979	325,485
	528,659	754,838	1,283,497
Discount, net	(2,147)		
Total	\$ 526,512		

### (e) Notes Payable to Third Parties

The outstanding balance of notes payable by the Commonwealth to third parties is comprised of the following (expressed in thousands):

#### Governmental activities:

U.S. Department of Housing and Urban Development (HUD) notes	\$ 1,030,667
Federal financial bank notes	10,634
Total notes payable to third parties – governmental entities	\$ 1,041,301
Notes payable to IBM – business-type activity	\$ 1,077

Both HUD and the federal financial bank notes are obligations of Public Housing Administration. The notes payable to HUD bear interest at rates ranging from 3.375% to 10%. Proceeds from these notes were used for the construction and modernization of the Commonwealth's public housing projects. These notes will be forgiven, together with accrued interest, when PRHA completes the certification and closing procedures of certain projects, and amends its annual contribution contract

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

with HUD. In the meantime, the notes continue accruing interest, which is capitalized into the notes principal balance. Since these notes carry no specific maturity, management has classified them as due within one year. The following presents the composition of the notes (expressed in thousands):

Principal balance	\$ 506,622
Accrued interest	<u>524,045</u>
Total	<u>\$ 1,030,667</u>

Presently, PRPHA is working to complete the aforementioned certifications and closing procedures. At June 30, 2003, no forgiveness of the notes had been granted by HUD.

The federal financial bank notes bear interest ranging from 10.62% to 16.16% and are payable in annual installments through November 2013. These notes are paid through annual contributions from the federal government as provided in the annual contribution contract with HUD. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 996	702	1,698
2005	1,060	638	1,698
2006	1,091	566	1,657
2007	1,163	494	1,657
2008	1,240	417	1,657
2009-2013	4,733	893	5,626
2014	<u>351</u>	<u>23</u>	<u>374</u>
Total	<u>\$ 10,634</u>	<u>3,733</u>	<u>14,367</u>

The notes payable to IBM are represented by an installment sales contract agreement entered into with the Lottery of Puerto Rico for the purchase of certain computer equipment. The sales contract agreement is payable in monthly installments of \$74,000, including interest at the rate of 5.62%, through July 2004.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### (f) *Notes Payable to Component Units*

The Commonwealth financed certain short- and long-term liabilities through GDB and other component units. The outstanding balance on the financing provided by GDB is comprised of the following (expressed in thousands):

Department of the Treasury	\$ 451,457
Public Building Authority	85,245
Puerto Rico Court Administration Office loan	43,460
Department of Agriculture loan	35,473
Note payable assumed from the Puerto Rico Housing Bank and Finance Agency	25,125
Department of Justice	18,533
Office of the Superintendent of the Capitol loan	14,511
Disaster assistance loan	12,055
Correction Administration loan	8,726
Department of Natural Resources	4,277
State Office for the Historic Conservation	2,556
Department of Education	<u>186</u>
Total debt due to GDB	<u>701,604</u>

The remaining outstanding balance on the financing provided by other component units is comprised of the following (expressed in thousands):

Health facilities agreement payable to the Medical Science Campus of the UPR	31,040
Note payable to Puerto Rico Electric Power Authority	<u>31,597</u>
Total debt due to other component units	<u>62,637</u>
Total – governmental activities	<u>\$ 764,241</u>
Line-of-credit agreement with GDB for the Traditional Lottery – business-type activities	<u>\$ 1,308</u>

During fiscal year 2003, the Department of the Treasury entered into various interim line-of-credit agreements with GDB amounting to approximately \$1.6 billion, which were drawn and repaid within the same year. The most significant line-of-credit agreement related to advances in anticipation of the issuance of the 2003 TRANS and for the repayment of the 2002 TRANS.

The PBA capital project fund had at June 30, 2003 advances outstanding from GDB in the amount of approximately \$85 million, represented by an interim construction line-of-credit agreement to finance the construction activities of PBA. These advances bear interest at 1.50% over the commercial paper issued by GDB (2.57% at June 30, 2003).

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

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During fiscal year 2003, the Department of the Treasury entered into various line-of-credit agreements with GDB amounting to a maximum of \$690 million for different purposes. The borrowings under these line-of-credit agreements bear interest predominantly at variable interest rates, payable annually until the maturity of such lines, which ranges from June 30, 2008 to October 31, 2032. The purpose, interest rate, maturity date, and amount outstanding under each individual agreement at June 30, 2003 consist of the following (expressed in thousands):

<u>Purpose</u>	<u>Interest rate</u>	<u>Maturity</u>	<u>Line of credit</u>	<u>Outstanding balance</u>
Replenishment of income tax refund reserve	125 bp over three- months LIBOR	June 30, 2008	\$ 250,000	250,000
Capital improvement projects of agencies and municipalities	150 bp over GDB's commercial paper rate	June 30, 2019	130,000	50,510
Financing additional resources to meet appropriations in annual budget of Commonwealth	8%	October 31, 2032	110,000	50,317
Financing agencies' old debts	125 bp over three- months LIBOR	September 30, 2012	100,000	45,470
Financing resources to meet appropriations related to agencies' old debts outstanding with PBA	125 bp over 3 months LIBOR	September 30, 2008	40,000	33,942
Acquisition of correctional facilities	125 bp over 3 months LIBOR	September 30, 2012	15,000	15,000
Information technology projects	150 bp over GDB's commercial paper rate	September 30, 2008	44,868	6,218
			<u>\$ 689,868</u>	<u>451,457</u>

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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On May 7, 2001, the Puerto Rico Court Administration Office (the Office) entered into a \$49.4 million nonrevolving line-of-credit agreement with GDB for operating purposes. Borrowings under this line-of-credit agreement bear interest at a variable rate of three-months London Interbank Offered Rate (LIBOR) plus 1%, not to exceed 8%. The Office must deposit \$6 million a year, from the total fees collected on the filing of civil cases, in a special fund created by the Department of the Treasury of the Commonwealth, which will be pledged for repayment until July 31, 2012. As of June 30, 2003, approximately \$43.5 million remain outstanding.

On August 9, 1999, the Department of Agriculture of the Commonwealth entered into a \$125 million nonrevolving line-of-credit agreement with GDB to provide economic assistance to the agricultural sector, which sustained severe damages caused by Hurricane Georges in 1998. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on September 30, 2004. As of June 30, 2003, \$35.5 million were outstanding. The line of credit will be repaid from future legislative appropriations.

Pursuant to Act No. 103 of August 11, 2001, the Housing Bank, formerly a discretely presented component unit of the Commonwealth, merged with and into the Puerto Rico Housing Finance Corporation, a blended component unit of GDB, which was redenominated as the Puerto Rico Housing Finance Authority. This legislation established that pursuant to the aforementioned merger, any residual amount of net assets of the Housing Bank would be transferred to the general fund of the Commonwealth. At the same time, a \$75 million line of credit that the Housing Bank had with GDB was also assumed by the general fund of the Commonwealth pursuant to this same legislation. This line of credit, bearing a variable interest rate is due on June 30, 2004. The amount outstanding at June 30, 2003 was \$25.1 million after a partial payment of \$37.3 million made during the year.

On October 2, 2002, the Department of Justice of the Commonwealth entered into a \$90 million line-of-credit agreement with GDB for the financing of 12 public improvements projects for the municipality of Ponce pursuant a court order. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line-of-credit on September 30, 2013. As of June 30, 2003, \$18.5 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On June 21, 2001, the Office of the Superintendent of the Capitol (Superintendent) entered into a \$10 million line-of-credit agreement with GDB for the construction of a parking lot. Borrowings under this line-of-credit agreement bear interest at a fixed rate of 8% and are payable from future legislative appropriations commencing in fiscal year 2003 through fiscal year 2006. As of June 30, 2003, \$9.9 million had been drawn from the line-of-credit agreement.

On February 15, 2002, the Superintendent entered into an additional \$10 million line-of-credit agreement with GDB for the acquisition and remodeling of several buildings under their jurisdiction. Borrowings under this line-of-credit agreement bear interest at a fixed rate of 8% and are payable

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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from future legislative appropriations commencing in fiscal year 2003 through fiscal year 2008. As of June 30, 2003, only \$4.6 million had been drawn from the line-of-credit agreement. Although the amount drawn through June 30, 2003 is expected to be repaid within one year, this line of credit is nevertheless classified as long term since the maximum amount of \$10 million, when drawn completely will be repaid in various installments through fiscal year 2008.

The disaster assistance loan of approximately \$93.9 million was used to repay a debt for such amount to the U.S. Federal Emergency Management Agency, which funded the Commonwealth's share of the relief grants for the residents of Puerto Rico affected by Hurricane Hugo in 1989. As of June 30, 2003, approximately \$12 million were outstanding. Debt service requirements in future years are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 11,552	603	12,155
2005	503	25	528
Total	<u>\$ 12,055</u>	<u>628</u>	<u>12,683</u>

On August 28, 2000, GDB approved an amendment to the terms of two lines-of-credit agreements of the Correction Administration by which such debts would be repaid between fiscal years 2000 and 2004. The two agreements were issued by GDB in August 1998 to partially fund permanent improvements to correctional facilities. The agreements have variable interest rate and limits of \$60 million and \$15 million. Their outstanding balance as of June 30, 2003 is \$8.7 million, which requires repayment in 2004. Interest repayment requirements are estimated in \$10,000 for 2004.

On August 21, 2002, the Department of Natural Resources of the Commonwealth entered into a \$22.7 million line-of-credit agreement with GDB for the canalization of the Bucaná River. Borrowings under this line of credit agreement bear interest at variable rates and are payable upon the maturity of the line-of-credit on June 30, 2005. As of June 30, 2003, \$4.3 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On August 1, 2001, the State Office for the Historic Conservation entered into a \$4.5 million line-of-credit agreement with GDB for the construction and conservation of the Santa Catalina Palace and the Real Audiencia building. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on December 31, 2008. As of June 30, 2003, \$2.6 million were outstanding. The line of credit will be repaid from future legislative appropriations.

On February 6, 2003, the Department of Education of the Commonwealth entered into a \$25 million line-of-credit agreement with GDB for the purchase of equipment and for school improvements. Borrowings under this line-of-credit agreement bear interest at variable rates and are payable upon the maturity of the line of credit on June 30, 2008. As of June 30, 2003, \$186,000 were outstanding. The line of credit will be repaid from future legislative appropriations.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

As of July 1, 1999, approximately \$102 million from various agreements with the UPR, a discretely presented component unit, in relation to outstanding noninterest-bearing debt accumulated in prior years by the former HFSA were transferred to the Commonwealth. As of June 30, 2003, approximately \$31 million are outstanding. Future amounts required to pay principal balances at June 30, 2003 are as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2004	\$ 7,570
2005	7,570
2006	—
2007	7,570
2008	8,330
Total	<u>\$ 31,040</u>

The noninterest-bearing note payable to PREPA, a discretely presented component unit, consists of approximately \$37.9 million of fuel adjustment subsidy due by the Commonwealth. The yearly amortization will vary depending on the gross electric sales for the year. The amortized amount for the year ended June 30, 2003 was approximately \$31.5 million. Future amounts required to pay principal balances at June 30, 2003 are as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2004	\$ 6,326
2005	6,327
2006	6,327
2007	6,327
2008	6,290
Total	<u>\$ 31,597</u>

The Department of the Treasury of the Commonwealth entered into a line-of-credit agreement with GDB for the purpose of financing the costs of lottery, a new series of tickets for the Lottery of Puerto Rico. The note establishes a credit line limit of \$2.5 million, maturing on July 1, 2007 and accruing interest at a rate of 6.5%. Annual interest payment commitments through 2007 are estimated in \$68,000. The amount outstanding as of June 30, 2003, is approximately \$1.3 million.

**(g) *Compensated Absences***

Long-term debt includes approximately \$1,154 million accrued vacations and sick leave benefits at June 30, 2003. The total liability of compensated absences recorded as governmental and business-type activities amounted to \$1,150 million and \$4 million, respectively.



# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

### (h) *Net Pension Obligation*

The amount reported as net pension obligation of approximately \$3.8 billion represents the cumulative amount owed by the Commonwealth for the unfunded prior years' actuarially required pension contributions to the ERS and the TRS (collectively known as the pension plans) (see note 19). The net pension obligation has been recorded as a liability in the governmental activity in the accompanying government-wide statement of net assets.

### (i) *Unpaid Lottery Prizes*

The amount reported as unpaid lottery prizes represents the lottery prizes payable of the Lottery of Puerto Rico (commonly known as Traditional Lottery) and the additional lottery system (commonly known as Lotto) jointly known as the Lottery Systems at June 30, 2003. The minimum annual payments related to unpaid awards of both lotteries are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 57,471	447	57,918
2005	26,772	5,004	31,776
2006	25,098	6,678	31,776
2007	23,472	8,272	31,744
2008	21,934	9,810	31,744
2009-2013	70,427	49,791	120,218
2014-2018	41,299	49,968	91,267
2019-2023	8,303	18,712	27,015
Total	<u>\$ 274,776</u>	<u>148,682</u>	<u>423,458</u>

The minimum annual payments related to unpaid prizes included expired tickets of approximately \$5 million in 2003.

The liability for unpaid lottery prizes is reported in the accompanying government-wide statement of net assets and the statement of net assets – business-type activities – enterprise funds.

### (j) *Liability for Insurance Benefits Claims*

The Commonwealth provides unemployment compensation, nonoccupational disability, and drivers' insurance coverage to public and private employees through various insurance programs administered by the Department of Labor and Human Resources of the Commonwealth. These insurance programs cover workers against unemployment, temporary disability, or death because of work or employment-related accidents, or because of illness suffered as a consequence of their employment.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

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The Commonwealth establishes liabilities for incurred but unpaid benefits and benefit adjustment expenses based on the ultimate cost of settling the benefits. Insurance benefit claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. The liability for insurance benefits claims is reported as a current liability in the accompanying government-wide statement of net assets and the statement of net assets – business-type activities – enterprise funds.

### (k) *Obligations Under Capital Lease Purchase Arrangements*

The Commonwealth is obligated under capital leases with third parties that expire through 2033 for land, buildings, and equipment. At June 30, 2003, the capitalized cost of the land, buildings, and equipment amounted to approximately \$186 million and is included in the accompanying government-wide statement of net assets within capital assets.

The present value of future minimum capital lease payments at June 30, 2003 reported in the accompanying government-wide statement of net assets is as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2004	\$ 23,707
2005	19,224
2006	17,117
2007	14,229
2008	13,850
2009-2013	66,449
2014-2017	65,478
2019-2022	56,934
2024-2028	56,934
2029-2033	<u>36,573</u>
Total future minimum lease payments	370,495
Less: amount representing interest costs	<u>207,524</u>
Present value of minimum lease payments	<u>\$ 162,971</u>

Leased land, buildings, and equipment under capital leases in capital assets at June 30, 2003, include the following (expressed in thousands):

Land	\$ 6,870
Buildings	147,293
Equipment	<u>31,899</u>
Subtotal	186,062
Less: accumulated amortization	<u>31,213</u>
Total	<u>\$ 154,849</u>

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Amortization charge applicable to capital leases and included within depreciation expense of capital assets amounted to approximately \$8.5 million in 2003.

The Commonwealth is also committed under numerous operating leases, covering land, office facilities, and equipment. Rental expenditures within the governmental funds for the year ended June 30, 2003 under such operating leases were approximately \$120 million.

The future minimum lease payments for these leases are as follows (expressed in thousands):

<u>Year ending June 30,</u>	
2004	\$ 73,652
2005	58,841
2006	35,967
2007	23,468
2008	8,274
2009-2013	14,113
2014-2018	5,717
2019-2023	4,650
2024-2028	861
Total future minimum lease payments	\$ <u>225,543</u>

### (l) *Other Long-Term Liabilities*

The remaining long-term liabilities include (expressed in thousands):

	<u>Governmental activities</u>	<u>Business-type activities</u>	<u>Total</u>
Employees' Christmas bonus	\$ 101,623	351	101,974
Liability for federal cost disallowances	52,089	—	52,089
Liability for legal claims and judgments	68,702	—	68,702
Other	2,582	—	2,582
Total	\$ <u>224,996</u>	<u>351</u>	<u>225,347</u>

### (m) *Advance Refunding, Defeased Bonds, and Refunding of Special Promissory Notes*

The Commonwealth advance refunded certain general obligation bonds through the issuance of approximately \$1,775 million of general obligation public improvements refunding bonds during the year ended June 30, 2003. The Commonwealth used approximately \$2,228 million from the net proceeds of the issued bonds and additional moneys from the Commonwealth to purchase U.S. government securities, which were deposited in an irrevocable trust fund with an escrow agent to provide for all future debt service payments of the refunded bonds. As a result, the refunded bonds are considered to be defeased, and the liabilities have therefore been removed from the statement of

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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net assets. As a result of this advance refunding, the Commonwealth decreased current year debt service payments and has taken advantage of lower interest rates, and it has increased its aggregate debt service payments by approximately \$102 million over the next 24 years and obtained an economic gain (the difference between the present values of the debt service payments of the refunded and refunding bonds) of approximately \$39.2 million. At June 30, 2003, approximately \$1,204 million of the bonds refunded during the year ended June 30, 2003 remain outstanding and are considered defeased.

In prior years, the Commonwealth also defeased certain general obligation and other bonds by placing the proceeds of bonds in an irrevocable trusts to provide for all future debt service payments on the refunded bonds. Accordingly, the trusts' account assets and liabilities for the defeased bonds are not included in the basic financial statements. At June 30, 2003, approximately \$2.6 billion of bonds outstanding from prior years advance refunding are considered defeased.

In addition, the PBA a blended component unit, has defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debts service payments on the old debts. Accordingly, the trust accounts assets and liabilities for the defeased bonds are not included in the statement of net assets. As of June 30, 2003, approximately \$1,477 million of PBA bonds are considered defeased.

During November 2001, the Department of Education of the Commonwealth issued a certification whereby certain Commonwealth public schools were designated as a "qualified zone academy" pursuant to Section 1397E of the U.S. Internal Revenue Code of 1986, as amended. On December 12, 2001, PFC, a blended component unit of GDB, issued \$96.8 million of Qualified Zone Academic Bonds (QZAB) to finance expenditures of the Department of Education of the Commonwealth under the aforementioned program, including rehabilitation and repairs of school buildings and other facilities, the development and implementation of academic curricula, technology training for some or all schools and the costs of issuance of the bonds. The QZAB are payable upon its maturity on December 11, 2015, since the federal government grants tax exemptions to bond holders in lieu of an interest rate. Simultaneous with the QZAB issuance, The Children's Trust, a blended component unit of the Commonwealth, granted \$47.2 million to the Department of Education of the Commonwealth, which in turn deposited the moneys to the credit of an escrow trust account invested in guaranteed investment contracts that will be used solely for the repayment in 2015 of the QZAB. The QZAB are considered defeased and the difference between the bonds amount and the amount deposited in the escrow account has been deferred, and is amortized into income over the term of the bonds.

#### **Fiduciary Funds**

On August 1, 1996, the TRS entered into a loan agreement with AFICA, a discretely presented component unit, to secure AFICA's issuance of \$26.9 million of industrial revenue term bonds. The bonds were issued under a trust agreement and are secured by a pledge of certain marketable securities of the TRS.

## COMMONWEALTH OF PUERTO RICO

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The proceeds from the sale of the bonds were lent by AFICA to TRS to finance the acquisition of certain buildings and related facilities and to pay certain expenses incurred in connection with the issuance and sale of the bonds.

Bonds payable outstanding at June 30, 2003, are as follows (expressed in thousands):

Term Bonds Series A payable through 2012, interest payable on a monthly basis at rates varying from 6.50% to 6.65%	\$ 8,345
Term Bonds Series B payable through 2022, interest payable semiannually at 5.50%	14,598
Total	<u>\$ 22,943</u>

Maturities of the term bonds are as follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 710	1,345	2,055
2005	755	1,296	2,051
2006	805	1,244	2,049
2007	855	1,189	2,044
2008	915	1,128	2,043
2009-2013	5,480	4,628	10,108
2014-2018	6,945	2,946	9,891
2019-2023	6,478	804	7,282
Total	<u>\$ 22,943</u>	<u>14,580</u>	<u>37,523</u>

The Series A and Series B Bonds are subject to redemption, at the option of the TRS, in whole or in part on July 1, 2006, or any date thereafter at the determined redemption prices, plus accrued interest to the redemption date as follows:

July 1, 2006 through June 30, 2007	102%
July 1, 2007 through June 30, 2008	101%
July 1, 2008 and thereafter	100%

#### Discretely Presented Component Units

Notes and bonds payable are those liabilities that are paid out of resources pledged by the other component units. These notes and bonds do not constitute a liability or debt of the Commonwealth.

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Notes payable outstanding at June 30, 2003 are as follows (expressed in thousands):

Component unit	Interest rate	Maturity through	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year
Government Development Bank for Puerto Rico	1.46%	2003	\$ 398,746	2,357,182	1,994,761	761,167	761,167
Puerto Rico Highway and Transportation Authority	5.74%	2035	300,000	—	300,000	—	—
Puerto Rico Electric Power Authority	LIBOR minus 3%	2005	5,000	—	—	5,000	—
State Insurance Fund Corporation	Discounted notes	2019	58,678	—	905	57,773	1,135
Economic Development Bank for Puerto Rico	1.48% – 6.90%	2026	144,494	133,000	116,943	160,551	5,317
Puerto Rico Industrial Development Company	6.625% – 6.8125%	2012	20,604	39,024	656	58,972	1,215
Puerto Rico Ports Authority	Variable	2005	15,000	32,800	738	47,062	25,162
Total notes payable – component units			\$ 942,522	2,562,006	2,414,003	1,090,525	793,996

Notes payable of \$125 million of PREPA, not included in the table above, have no fixed maturity date and variable interest rates. For financial reporting purposes, these notes have been classified as due within one year. These had no additions or reductions during 2003.

Debt service requirements on component units' notes payable with fixed maturities at June 30, 2003, were as follows (expressed in thousands):

Year ending June 30,	Principal	Interest	Total
2004	\$ 793,996	11,024	805,020
2005	84,732	11,646	96,378
2006	2,938	11,311	14,249
2007	3,585	11,104	14,689
2008	4,197	10,865	15,062
2009-2013	27,833	49,584	77,417
2014-2018	79,209	38,205	117,414
2019-2023	90,711	22,708	113,419
2024-2028	3,324	229	3,553
Total	\$ 1,090,525	166,676	1,257,201

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

June 30, 2003

Commonwealth appropriation bonds payable outstanding at June 30, 2003 are as follows (expressed in thousands):

Component unit	Interest rate	Maturity through	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year
Puerto Rico Aqueduct and Sewer Authority	4% – 6.15%	2031	\$ 712,130	—	—	712,130	7,273
Tourism Company of Puerto Rico	4% – 6.15%	2031	127,115	193	—	127,308	1,302
Land Authority of Puerto Rico	4% – 6.15%	2031	111,058	3	—	111,061	1,134
Government Development Bank for Puerto Rico	4% – 6.15%	2031	10,029	—	—	10,029	102
Puerto Rico Infrastructure Financing Authority	4% – 6.15%	2031	10,331	—	—	10,331	106
Puerto Rico Solid Waste Authority	4% – 6.15%	2031	15,521	6,763	292	21,992	228
Total appropriation bonds – component units			\$ 986,184	6,959	292	992,851	10,145

Debt service requirements on component units' appropriation bonds payable with fixed maturities at June 30, 2003, were as follows (expressed in thousands):

Year ending June 30,	Principal	Interest	Total
2004	\$ 10,145	56,036	66,181
2005	10,141	55,583	65,724
2006	2,533	55,434	57,967
2007	1,829	55,340	57,169
2008	13,060	54,686	67,746
2009-2013	76,852	261,555	338,407
2014-2018	98,008	239,213	337,221
2019-2023	140,226	199,111	339,337
2024-2028	303,621	144,930	448,551
2029-2033	336,436	18,004	354,440
Total	\$ 992,851	1,139,892	2,132,743

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## Notes to Basic Financial Statements

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Bonds payable outstanding at June 30, 2003 are as follows (expressed in thousands):

Component unit	Interest rate	Maturity through	Beginning balance	Additions	Reductions	Ending balance	Amounts due within one year
Government							
Development Bank for Puerto Rico	5% – 6.25%	2006	\$ 1,487,318	452,616	168,264	1,771,670	84,390
Puerto Rico Infrastructure Financing Authority	Variable	2028	2,008,375	—	23,484	1,984,891	24,580
University of Puerto Rico	3% – 5.75%	2030	450,511	—	18,226	432,285	21,170
Puerto Rico Municipal Finance Authority	5% – 8.62%	2023	957,339	534,620	67,849	1,424,110	85,636
Puerto Rico Ports Authority	5% – 7.30%	2021	89,985	—	7,728	82,257	8,380
Puerto Rico Aqueduct and Sewer Authority	3.5% – 8.22%	2040	834,470	—	15,720	818,750	7,583
Puerto Rico Highway and Transportation Authority	Various	2041	4,482,415	1,720,099	888,120	5,314,394	10,435
Puerto Rico Industrial Development Company	5.375% – 7.75%	2021	184,033	2,481	9,269	177,245	9,585
Puerto Rico Electric Power Authority	3.8% – 7%	2031	4,627,928	—	121,210	4,506,718	285,407
Total bonds – component units			\$ 15,122,374	2,709,816	1,319,870	16,512,320	537,166

Debt service requirements on component units' bonds payable with fixed maturities at June 30, 2003, were as follows (expressed in thousands):

Year ending June 30,	Principal	Interest	Total
2004	\$ 537,166	490,281	1,027,447
2005	58,090	477,042	535,132
2006	61,885	465,251	527,136
2007	65,105	453,236	518,341
2008	67,701	442,442	510,143
2009-2013	382,031	844,387	1,226,418
2014-2018	393,650	616,866	1,010,516
2019-2023	435,380	433,794	869,174
2024-2028	1,808,369	276,620	2,084,989
2029-2033	250,943	157,064	408,007
2034-2038	256,335	91,067	347,402
2039-2043	12,214,997	16,460	12,231,457
Total	16,531,652	4,764,510	21,296,162
Less: discounts, net	(19,332)		
	\$ 16,512,320		



## COMMONWEALTH OF PUERTO RICO

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Several component units have defeased certain revenue bonds by placing the proceeds of new bonds in irrevocable trusts to provide for all future debt service payments on the old debts. Accordingly, the trust accounts assets and liabilities for the defeased bonds are not included in the statement of net assets. As of June 30, 2003, the following bonds are considered defeased which pertain to major component units:

	<b>Amount outstanding at June 30, 2003 (in millions)</b>
Puerto Rico Highway and Transportation Authority	\$ 1,152
Puerto Rico Electric Power Authority	614

#### (15) Guaranteed and Appropriation Debt

##### (a) *Guaranteed Debt*

The Commonwealth may provide guarantees for the repayment of certain borrowings of component units to carry out designated projects. At June 30, 2003, the following component unit debts are guaranteed by the Commonwealth (expressed in thousands):

	<b>Maximum guarantee</b>	<b>Outstanding balance</b>
Blended component unit:		
Public Buildings Authority	\$ 2,100,000	2,097,930
Discretely presented component units:		
Puerto Rico Aqueduct and Sewer Authority	673,790	456,638
Government Development Bank for Puerto Rico	625,000	267,000
Total	<u>\$ 3,398,790</u>	<u>2,821,568</u>

The Commonwealth has guaranteed the payments of rentals of its departments, agencies, and component units to PBA, a blended component unit, under various lease agreements executed pursuant to the law that created PBA. Such rental payments include the amounts required by PBA for

# COMMONWEALTH OF PUERTO RICO

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the payment of principal and interest on the guaranteed debt as authorized by law. The rental commitment to cover principal and interest on the guaranteed debt (excluding discounts) as of June 30, 2003 and for the next five years and thereafter follows (expressed in thousands):

<u>Year ending June 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 33,075	108,235	141,310
2005	26,276	110,265	136,541
2006	53,980	109,159	163,139
2007	56,855	109,448	166,303
2008	73,057	95,949	169,006
2009-2013	419,447	434,006	853,453
2014-2018	382,170	336,035	718,205
2019-2023	298,990	241,433	540,423
2024-2028	295,490	167,916	463,406
2029-2033	256,619	123,780	380,399
2034-2037	190,569	20,681	211,250
Total	<u>\$ 2,086,528</u>	<u>1,856,907</u>	<u>3,943,435</u>

Rental income of PBA funds amounted to approximately \$228 million during the year ended June 30, 2003, of which \$115 million was used to cover debt service obligations.

Act 45 of July 28, 1994, states that the Commonwealth guarantees the payment of principal and interest of all outstanding bonds at the date the law was enacted and of all future bond issues to refinance those outstanding bonds of PRASA. During December 1995, PRASA issued refunding bonds to refinance all outstanding bonds amounting to approximately \$400.3 million. The outstanding balance of these refunding bonds at June 30, 2003, amounted to \$318 million. Act No. 140 of August 3, 2000, amended Act No. 45 to extend the Commonwealth guarantee to include the principal and interest payments of the Rural Development Serial Bonds and the loans under the State Revolving Fund Program (SRFP) outstanding at the effective date of Act No. 140, and of all future bonds and SRFP loans that may be issued until June 30, 2005. The outstanding balance of the Rural Development Serial Bonds and SRFP loans at June 30, 2003 amounted to \$139 million and \$138 million, respectively.

The Commonwealth guarantees the Adjustable Refunding Bonds, Series 1985, issued by GDB, a discretely presented component unit. The outstanding balance of these bonds amounts to \$267 million at June 30, 2003.

The Housing Bank, a former component unit of the Commonwealth, which merged with and into GDB during 2002, insured mortgages granted to low- and moderate-income families through its mortgage loan insurance program. The Commonwealth guarantees up to \$75 million of such mortgage loans. As of June 30, 2003, the mortgage loan insurance program was insuring loans aggregating \$421 million. Currently, the Commonwealth has not been called to make any direct payments pursuant to these guarantees.

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#### *(b) Appropriation Debt*

At June 30, 2003, the outstanding balances of debt payable by government appropriations and which are included in the individual financial statements of these entities are as follows (expressed in thousands):

Discretely presented component units:

Puerto Rico Aqueduct and Sewer Authority	\$ 1,140,291
Puerto Rico Infrastructure Financing Authority	955,087
Government Development Bank for Puerto Rico	340,238
Tourism Company of Puerto Rico	233,116
Land Authority of Puerto Rico	154,994
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	128,302
Puerto Rico Solid Waste Authority	29,549
National Parks Company of Puerto Rico	11,357
Special Communities Perpetual Trust	4,952
Employment and Training Enterprises Corporation	2,135
Other governmental entities	38,005
	<u>\$ 3,038,026</u>

#### **(16) Conduit Debt Obligations**

From time to time, certain of the Commonwealth's component units issue revenue bonds to provide financial assistance to private-sector entities for the acquisition and construction of transportation, environmental, industrial, tourism, educational, commercial facilities, and Caribbean Basin projects deemed to be in the public interest and that are expected to provide benefits to Puerto Rico. These bonds are secured by the property financed and are payable solely from payments received on the underlying mortgage loans. Upon repayment of the bonds, ownership of the acquired facilities is retained by the private-sector entity served by the bond issuance. Neither the Commonwealth, nor any political subdivision or component unit thereof is obligated in any manner for the repayment of the bonds. Accordingly, the bonds are not reported as liabilities in the basic financial statements of the issuing

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entities. As of June 30, 2003, conduit debt obligations consisted of the following bonds issued by component units (expressed in thousands):

<u>Issuing entity</u>	<u>Issued since inception to date</u>	<u>Amount outstanding</u>
Discretely presented component units:		
Caribbean Basin Projects Financing Authority	\$ 676,000	22,000
Puerto Rico Ports Authority	\$ 155,410	155,410
Puerto Rico Highway and Transportation Authority	\$ 117,000	143,948
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	\$ 5,844,000	2,742,000

**(a) Caribbean Basin Projects Financing Authority (CBPFA)**

Pursuant to the loan agreements covering the issuance of these bonds, the proceeds from the sales were borrowed from CBPFA by corporations and partnerships operating in qualified Caribbean Basin countries. The revenue bonds are special and limited obligations of CBPFA and, except to the extent payable from bond proceeds and investments thereof, will be payable solely from and secured by a pledge and assignment of the amounts payable under the loan agreements between CBPFA and the borrowers. Furthermore, payment of the principal and interest on the revenue bonds is unconditionally guaranteed by the borrowers, their parent companies, and/or letters of credit from major U.S. banks or U.S. branches of international banks. The revenue bonds do not constitute a debt or a pledge of the good faith and credit of CBPFA or the Commonwealth or any political subdivision thereof.

**(b) Puerto Rico Ports Authority**

PRPA issued Special Facilities Revenue Bonds (1993 Series A) under the provisions of a trust agreement between PRPA and a private bank. The proceeds from the sale of the bonds were used to finance the construction of facilities, acquisition of equipment, and improvements to the Luis Muñoz Marín International Airport, for the benefit of a major private airline. The property is owned by PRPA and leased to the private company. Pursuant to the agreement between PRPA and the private company, the bonds will be paid from the rent collected from the airline in amounts sufficient to pay principal, premium (if any), and interest on the bonds. The airline has guaranteed these payments.

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**(c) *Puerto Rico Highway and Transportation Authority (PRHTA)***

In March 1992, PRHTA issued Special Facility Revenue Bonds for approximately \$117 million for the construction of a toll bridge. The proceeds from the sale of these bonds were transferred by PRHTA to a private entity, pursuant to a signed agreement for the construction, transfer, and operation of the bridge. The bonds shall be paid from the proceeds received by the private entity from the operation of the bridge. However, under certain circumstances, the private entity may have the right of terminating the agreement and PRHTA will assume the obligation to pay the bonds. The outstanding balance of these bonds at June 30, 2003 included accreted interest.

**(d) *AFICA***

The revenue bonds of AFICA are used to finance facilities for environmental control, development of industrial and commercial companies, tourism projects, hospitals, and educational facilities. Pursuant to the loan agreements, the proceeds from the sales were borrowed by corporations and partnerships operating in Puerto Rico. The bonds are limited obligations of AFICA and, except to the extent payable from bond proceeds and investment thereof, will be payable solely from and secured by a pledge and assignment of the amounts payable under the loan agreements between AFICA and each borrower. Furthermore, payment of the principal and interest on the revenue bonds is unconditionally guaranteed by each of the borrowers, their parent companies, or letters of credit from major U.S. banks or U.S. branches of international banks.

**(17) Risk Management**

The risk management program of the Commonwealth and most of its discretely component units are described in note 1(y). The following describes the risk management programs separately administered by certain discretely presented component units.

**(a) *UPR***

The UPR is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The UPR carries commercial insurance for these risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

Under Act No. 98 of August 24, 1994, the responsibility of UPR on medical malpractice claims is limited to a maximum amount of \$75,000 per person, or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Self-insured risks liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred

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but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount. Claim liabilities are reevaluated periodically to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. Changes in the claim liabilities amount for the current and prior fiscal years were as follows (expressed in thousands):

	<u>2003</u>	<u>2002</u>
Claims payable at beginning of year	\$ 12,755	13,465
Incurred claims and changes in estimates	2,969	4,043
Net payments for claims and adjustment expenses	<u>(2,366)</u>	<u>(4,753)</u>
Claims payable at end of year	<u>\$ 13,358</u>	<u>12,755</u>

Claims payable are reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

**(b) PREPA**

PREPA is exposed to various risks of losses related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Under the property and liability insurance program, PREPA provides coverage, among other things, for up to a maximum of \$250,000 for each general and liability claim, and \$2 million for each boiler and machinery and property liability claim. In addition, the property liability policy imposes windstorm and earthquake deductibles at 2% and 5% of the location's value subject to a maximum deductible of \$25 million per occurrence. PREPA purchases commercial insurance for claims in excess of coverage provided through the property and liability insurance program. PREPA considers its self-insurance fund adequate to provide for its self-insurance risk. Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated.

In addition, PREPA is self-insured for damage to its transmission and distribution lines. Transmission and distribution lines amounted to approximately \$3 billion at June 30, 2003 and 2002. PREPA's self-insurance fund provides for its self-insurance risk. This fund represents principally net assets and restricted assets set-aside for self-insurance amounting to approximately \$80.2 million and \$77.4 million as of June 30, 2003 and 2002, respectively.

PREPA has a cost plus health insurance program covering substantially all its employees. PREPA contracted an administrator for the processing, approval, and payment of claims at cost plus an administrative fee. The accrual includes claims processed and an estimate for claims incurred but not reported.

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Changes in the balances of the health insurance program and other self-insurance risks for the current and prior fiscal years were as follows (expressed in thousands):

	<u>2003</u>	<u>2002</u>
Claims payable at beginning of year	\$ 38,768	46,822
Incurred claims	116,545	90,269
Claims payment	<u>(104,422)</u>	<u>(98,323)</u>
Claims payable at end of year	<u>\$ 50,891</u>	<u>38,768</u>

Claims payable is reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

(c) **PRASA**

PRASA is exposed to various risks of losses related to torts; thefts of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Under the property insurance program, PRASA has a \$200 million blanket insurance on all real and personal property. The deductible for windstorm and flood is 2% and 5% for earthquake with a maximum amount of \$5 million. All other perils have a deductible of \$100,000 per occurrence except underground perils which have a \$1.5 million deductible.

The comprehensive general liability and automobile liability has basic limits of \$3 million and the umbrella is \$50 million per occurrence. The general liability coverage has a deductible of \$100,000 subject to an annual stop loss limit of \$2.25 million.

The boiler and machinery policy has an \$18 million aggregate coverage, the directors and officers' liability policy has a \$12 million aggregate coverage, the travel/accident policy has a \$2 million aggregate coverage, and the accident and health driver's policy has \$250,000 aggregate coverage.

Also, crime insurance policy is provided with \$1 million fidelity bond, and an insurance coverage of \$500,000 for the premises, transit, and depositors' forgery. There is a sublimit of \$20,000 for money orders and counterfeit currency coverage.

PRASA's insurance program is carried out by insurance brokers in coordination with PRASA's insurance office. Claims and liabilities are accounted for when it is probable that a claim has occurred and the amount of loss can be reasonably estimated. For the years ended June 30, 2003 and 2002, PRASA had a claims liability amounting to \$1.9 million and \$1.1 million, respectively, for insurance claims incurred but not reported.

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PRASA has a cost plus health insurance program covering its managerial employees. The plan administrator has a contract for the processing, approval, and payment of claims at cost plus an administrative fee. PRASA incurred health insurance claims, including an estimate for incurred but not reported claims, of approximately \$3.3 million for the year ended June 30, 2002. For the year 2003 no cost of health insurance claims were incurred by PRASA.

**(d) SIFC**

SIFC provides workers' compensation insurance to public and private employees. This insurance covers workers against injuries, disability, or death because of work or employment-related accidents, or because illness is suffered as a consequence of their employment. SIFC establishes liabilities for incurred but unpaid benefits and benefit adjustment expenses based on the ultimate cost of settling the benefits. The following table provides a reconciliation of the beginning and ending liability for incurred but unpaid benefits and benefit adjustment expenses for the years ended June 30, 2003 and 2002 (expressed in thousands):

	<u>2003</u>	<u>2002</u>
Liability for incurred but unpaid benefits and benefit adjustment expenses at beginning of year	\$ <u>939,623</u>	<u>946,431</u>
Incurred benefits related to:		
Insured events of the current year	181,381	223,771
Insured events of prior years	<u>100,137</u>	<u>162,356</u>
Total incurred benefits	<u>281,518</u>	<u>386,127</u>
Benefit payments related to:		
Insured events of the current year	207,575	218,825
Insured events of prior years	<u>148,214</u>	<u>174,110</u>
Total benefit payments	<u>355,789</u>	<u>392,935</u>
Liability for incurred but unpaid benefits and benefit adjustment expenses at end of year	\$ <u><u>865,352</u></u>	<u><u>939,623</u></u>

The liability for incurred but unpaid benefits and benefit adjustment expenses is reported as accounts payable and accrued liabilities in the accompanying statement of net assets.

The liability for compensation benefits is based on historical claims experience data, assumptions and projections as to future events, including claims frequency, severity, persistency, and inflationary trends determined by an independent actuary. The liability for benefits and expenses payable has been discounted at 2% and 3% in 2003 and 2002, respectively. The actuarial study considered the experience of SIFC from fiscal years 1988-1989 to 2002-2003, and included



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estimates for cases reported that have not been adjudicated and cases incurred but not reported. The actuarial study also included estimates for medical benefits, benefit adjustment expenses, and reimbursement of premiums. The assumptions used in estimating and establishing the liability are reviewed annually based on current circumstances and any adjustments resulting thereof are reflected in operations in the current period.

(e) **AACA**

AACA operates a system of compulsory insurance for vehicles licensed to be used on public roads and highways in Puerto Rico. This insurance covers death and bodily injuries caused by automobile accidents. The annual premium is \$35 per motor vehicle.

SIFC establishes liabilities for future benefits based on the ultimate cost of settling the benefits.

The following table provides a reconciliation of the beginning and ending liability for future benefits for the years ended June 30, 2003 and 2002 (expressed in thousands):

	<u>2003</u>	<u>2002</u>
Liability for future benefits at beginning of year	\$ 110,700	111,679
Incurred benefits related to:		
Insured events of the current year	73,329	55,772
Insured events of prior years	<u>(10,885)</u>	<u>(692)</u>
Total incurred benefits	<u>62,444</u>	<u>55,080</u>
Benefit payments related to:		
Insured events of the current year	24,208	23,044
Insured events of prior years	<u>35,374</u>	<u>33,015</u>
Total benefit payments	<u>59,582</u>	<u>56,059</u>
Liability for future benefits at end of year	\$ <u>113,562</u>	<u>110,700</u>

The liability for future benefits is reported as account payable and accrued liabilities in the accompanying statement of net assets. AACA has recorded this liability, including administrative expenses for claim processing, based on the results of actuarial reports prepared by independent actuaries, determined under two different methods. Death, funeral, disability, dismemberment, and the basic medical hospitalization liabilities were determined using a triangulation method. The extended benefits medical hospitalization reserve uses regression methodology to predict the ultimate incurred claims for each incurred calendar quarter. Additionally, assumptions are made about the mortality rates of the extended benefit claimants, recognizing the impact of their traumatic injuries on life span.

Changes in the ultimate liabilities for benefit payments may be required as information develops which varies from experience, provides additional data, or, in some cases augments data, which previously were not considered sufficient for use in determining the claim liabilities.

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*(f) PCSDIPRC*

The activity in the liability for possible losses on shares and deposits insured by PCSDIPRC during the years ended June 30, 2003 and 2002 was as follows (expressed in thousands):

	<u>2003</u>	<u>2002</u>
Balance at beginning of year	\$ 28,253	24,000
Provision for losses on shares and deposits for the year	4,108	3,960
Claim payments	(107)	(35)
Recoveries	746	328
Balance at end of year	<u>\$ 33,000</u>	<u>28,253</u>

**(18) Commitments and Contingencies**

*Primary Government*

The Commonwealth is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended, persons are authorized to sue the Commonwealth only for causes of actions set forth in said Act to a maximum amount of \$75,000 or \$150,000 if it involves actions for damages to more than one person or where a single injured party is entitled to several causes of action. Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Commonwealth may provide its officers and employees with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the payment of such judgments.

With respect to pending and threatened litigation, excluding the litigation mentioned in the following paragraph, the Commonwealth reported approximately \$69 million as an amount to cover for awarded and anticipated unfavorable judgments at June 30, 2003. This amount was included as other long-term liabilities in the accompanying statement of net assets, and represents the amount estimated as a probable liability or a liability with a fixed or expected due date that will require future available financial resources for its payment. Management believes that the ultimate liability in excess of amounts provided, if any, would not be significant.

The Commonwealth and various component units are defendants in lawsuits alleging violations of civil rights. Preliminary hearings and discovery proceedings are in progress. The amounts claimed exceed \$7.1 billion; however, the ultimate liability cannot be presently determined. It is the opinion of management that the claims are excessive and exaggerated. No provision for any liability that may result upon adjudication of these lawsuits have been recognized in the basic financial statements by the Commonwealth. Management believes that the ultimate liability in excess of amounts provided, if any, would not be significant.

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During fiscal year 1997, the PBA's employees filed a claim requesting the payment of vacation leave amounts earned plus penalties as required by statute for such amounts not paid in accordance with the applicable laws. As of June 30, 2003, there is an accrual of \$1.3 million for the settlement of this case. In addition, PBA is defendant and/or co-defendant in various lawsuits for alleged breach of contracts and other actions arising in the ordinary course of business, for which an accrual of \$3.7 million has been recorded.

The Commonwealth's PHA terminated certain management services contracts for the administration of certain public housing projects. As a result, plaintiffs are claiming approximately \$40 million in compensation for damages for alleged breach of contract. The management of PHA has established a liability for an estimated loss of approximately \$6 million.

The PRMSA, a blended component unit, is a defendant in industry-wide lawsuits filed on behalf of seamen or their personal representatives alleging injury or illness based upon exposure to asbestos or other toxic substances. The Authority has accrued approximately \$4 million at June 30, 2003 to cover the estimated liability that may arise from the current cases filed with the courts.

On July 6, 2001, PHA delivered possession of the assets and projects of its HOPE VI Program to HUD, as a result of an audit report by the HUD Office of Inspector General in which they are questioning \$20 million in federal financial assistance applicable to the HOPE VI Program, Comprehensive Grant Program, and Economic Development and Supportive Services Program related to the revitalization initiative of an area known as the New San Juan Gateway, covering the period from April 1995 to December 1999.

The Commonwealth receives financial assistance from the federal government in the form of grants and entitlements. Receipt of grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal law and regulations, including the expenditure of resources for eligible purposes. Substantially all grants are subject to audit under Circular A-133 of the OMB of the United States of America (OMB Circular A-133), all of which are performed at the individual agency level. Disallowance as a result of these audits may become liabilities of the Commonwealth. At June 30, 2003, based on an evaluation of pending federal disallowances, the Commonwealth has recorded approximately \$52 million as other long-term liabilities in the accompanying statement of net assets.

Construction commitments at June 30, 2003 for the PBA, a blended component unit, amounted to approximately \$280 million. In addition, the Commonwealth's construction commitments for public housing facilities amounted to approximately \$230 million at June 30, 2003.

At June 30, 2003, The Children's Trust, a blended component unit of the Commonwealth, had approved commitments to provide assistance to several entities through 63 contracts with balances amounting to approximately \$359.4 million.

On November 23, 1998, a global settlement agreement (the Agreement) was entered into by and between certain tobacco companies and certain states, territories, and other jurisdictions of the United States of America, including the Commonwealth. The Agreement calls for annual payments through the year 2025, which will vary due to inflationary and volume adjustments. After 2025, the tobacco companies are to continue making contributions in perpetuity. Pursuant to Act No. 173 of July 30, 1999, which created The

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Children's Trust, the Commonwealth assigned and transferred to The Children's Trust all payments that the Commonwealth is entitled to receive under the Agreement. Payments received under the Agreement and recognized as revenue during the year ended June 30, 2003 amounted to approximately \$102 million. Following is a summary of estimated payments to be received by The Children's Trust through the year ending June 30, 2025 (expressed in thousands):

<u>Year ending June 30,</u>	
2004	\$ 72,696
2005	73,642
2006	74,845
2007	75,990
2008	89,952
Thereafter	<u>1,742,195</u>
Total	<u>\$ 2,129,320</u>

#### *Component Units*

In the normal course of their operations the various component units are subject to guarantees, actions brought by third parties seeking damages or entering into commitments. Such actions are disclosed in the separately issued reports of the component units some of which are summarized below:

#### *General Commitments and Contingencies*

##### *(a) GDB*

At June 30, 2003, GDB has financial guarantees for public entities for approximately \$83.4 million and for private sector of approximately \$682.2 million. In addition, standby letters of credit to public entities were approximately \$85.7 million and to private sector were approximately \$113.4 million. Commitments to extend credit to public entities were approximately \$3.4 billion and to private sector were approximately \$32.3 million

GDB enters into sales of securities under agreements to repurchase. These agreements generally represent short-term debts and are presented as a liability in the statement of net assets. The securities underlying these agreements are usually held by the broker, or its agent, with whom the agreement is transacted. As of June 30, 2003, there were agreements outstanding for \$190 million and during the year the average amount outstanding was approximately \$216 million, the maximum amount outstanding at any month-end was approximately \$250 million; and the weighted average interest rate for the year and at year-end was approximately 1.65% and 1.09%, respectively.

GDB issues commercial paper in the U.S. taxable and tax exempt commercial paper markets, the Euro-dollar commercial paper market and to corporations that have tax exemption under the Commonwealth's Industrial Incentives Act and qualify for benefits provided by the U.S. Internal Revenue Code Section 936. Commercial paper represents unsecured obligations of GDB. The

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carrying amount of commercial paper at June 30, 2003 was approximately \$761 million, which also was the maximum amount at any month end; the weighted average amount outstanding during the year was approximately \$438 million and the weighted average interest rate for the year and at year-end was approximately 1.25% and 103%, respectively.

At June 30, 2003, GDB had outstanding interest rate swap agreements with other financial institutions in the aggregate notional amounts of \$637 million, having a fair value (payable position) of approximately \$46 million. GDB also had an equity appreciation index embedded in a \$200 million certificate of indebtedness. Such embedded derivative has been recognized as a liability at its fair value of approximately \$16 million as of June 30, 2003. GDB is exposed to credit loss in the event of nonperformance by the other parties to swap agreements. However, GDB does not anticipate nonperformance by counterparties.

On November 21, 2002, the Legislature of the Commonwealth approved Joint Resolution No.1027, authorizing GDB to transfer \$500 million as a contribution to SCPT, a discretely presented component unit created for the purpose of financing a variety of initiatives, primarily housing and infrastructure, directed to the betterment of disadvantage communities across the island. As approved in the Joint Resolution, the contribution will be disbursed following approved laws and regulations. The board of director of GDB approved a regulation (the regulation), which calls for the disbursement of contributions based on the compliance with certain reimbursement requirements. As of June 30, 2003, disbursements amounted to \$500,000.

**(b) PRHTA**

As part of the PRHTA's Urban Train project, a number of contractors have presented claims related to the project. Claims which are at various stages of analysis amount to approximately \$79 million as of June 30, 2003. From this amount, approximately \$12 million have been categorized as merited claims. Therefore, these amounts were included as accounts payable. The effect of the resolution of these claims, if any, in future years would be to increase the amounts being capitalized for the Urban Train project and increase the accounts payable in the accompanying statement of net assets.

**(c) PREPA**

In May 1998, the Municipality of Ponce (the Municipality) filed a complaint against PREPA in the San Juan Superior Court requesting the payment by PREPA of the full contributions in lieu of taxes and electric energy sales set aside for prior fiscal years. The complaint challenges the application by PREPA of the "net revenue" formula which reduced the amount available to pay contributions in lieu of taxes and electric energy sales set aside for the Municipality. Since the filing of this lawsuit by the Municipality, other municipalities have filed similar claims. PREPA understands it has applied and interpreted the "net revenue" formula in accordance with the enabling act which created PREPA. On April 14, 2003, PREPA made a settlement offer consisting of a payment in cash of \$68 million and

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\$57 million for electric infrastructure projects in the municipalities. As part of the settlement, the municipalities supported an amendment to the Act that was proposed by PREPA, that the amount payable to the municipalities is calculated based on a percentage of the net revenue defined on the 1974 Agreement.

**(d) PRIFA**

The law that created PRIFA (as amended) requires that the first \$70 million up to fiscal year 2023 of federal excise taxes received by the Commonwealth be transferred to PRIFA for deposit to PRIFA's infrastructure fund (the Infrastructure Fund). Federal excise taxes consist of taxes received by the Commonwealth from the United States in connection with rum and other articles produced in Puerto Rico and sold in the United States that are subject to federal excise tax.

A related trust agreement requires PRIFA to deposit to the credit of a sinking fund the federal excise taxes and other moneys deposited to the credit of the Infrastructure Fund in such amounts as are required to meet debt service requirements with respect to the bonds. Rum is the only article currently produced in Puerto Rico subject to federal excise tax, the proceeds of which are required to be transferred from the federal government to the Commonwealth.

The federal excise taxes securing the bonds are subject to a number of factors, including the continued imposition and remittance of such taxes to the Commonwealth and conditions affecting the Puerto Rico rum industry. If the federal excise taxes received by the Commonwealth in any fiscal year are insufficient to deposit the amount required by the act into the Infrastructure Fund, the act requires that PRIFA request, and the director of the OMB include in the annual budget of the Commonwealth for the corresponding fiscal year, an appropriation necessary to cover such deficiency. The Commonwealth's Legislature, however, is not legally obligated to make the necessary appropriation to cover such deficiency.

**(e) PRTA**

PRTA, through its subsidiary PRTA Holdings, holds shares of Telecomunicaciones de Puerto Rico, Inc. (TELPRI). TELPRI is the Puerto Rico corporation that was organized for the purpose of acquiring the stock of Puerto Rico Telephone Company (PRTC) and Celulares Telefónica (CT) from PRTA in connection with the sale transaction of March 2, 1999, where a subsidiary of Verizon, Popular, Inc., and TELPRI's employee stock ownership plan acquired 57% of TELPRI and completed the privatization of PRTC and CT. It is contemplated that all shares of TELPRI held by PRTA Holdings will be sold in public offerings and private placements, and all dividends and proceeds received from the sale of the shares will be distributed to the ERS.

Verizon delivered a notice of claim for indemnity to PRTA related to certain alleged actions of PRTA that occurred before the closing of the sale transaction described above. The amount of indemnity sought by Verizon is approximately \$105 million, related to several matters including PRTC's exposure to a potential reduction in tariffs or required rebate to clients as a result of an

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adverse decision by the Federal Communications Commission (FCC) on a regulatory matter. The FCC's decision has been appealed by PRTC and is awaiting a determination by the FCC. Additionally, in connection with the privatization, the PRTA agreed to indemnify, defend, and hold TELPRI harmless for specified litigation in excess of \$50 million in the aggregate.

On March 2, 1999, PRIFA received \$1.2 billion in connection with the sale of certain assets of PRTA, which were deposited in a corpus account, which principal may not be reduced for any reason, and that income received from the investment of moneys in a corpus account and other moneys received may be deposited in additional accounts. Moneys deposited in the additional accounts are to be used first to pay the principal and interest of any bonds outstanding or to be issued by PRIFA and then for the expansion, development, and modernization of infrastructure related to the aqueduct and sewer systems of Puerto Rico.

#### *(f) UPR*

The UPR participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of OMB Circular A-133, or to compliance audits by federal grantor agencies. Although these programs have been audited through June 30, 2000 under OMB Circular A-133, and through various dates by grantor agencies, the resolution of certain previously identified questioned costs has not been resolved. The amount, if any, of expenditures which may be disallowed by the federal grantor agencies cannot be determined at this time, although the UPR's management expects such amounts, if any, will be immaterial.

Desarrollos Universitarios, Inc. (Desarrollos) was incorporated on October 2, 1996. Desarrollos is a nonprofit corporation, with the sole purpose of developing, constructing, and operating academic, residential, administrative, office, commercial, and maintenance facilities (Plaza Universitaria) for use by students, faculty members, administrators, employees, visitors, invitees, and other members of or persons and entities related to or conducting business with the UPR community, or other activities conducted in such facility. On May 11, 2000, UPR's board of trustees ratified a Memorandum of Agreement (MOA) to establish a contractual agreement between the UPR and Desarrollos. The MOA, dated May 22, 1998, states among other things the following: (1) the UPR will lease to, or otherwise grant to, Desarrollos the right for the long-term use of the land, for the sole purpose of developing, constructing, and operating Plaza Universitaria; (2) Desarrollos shall finance the development of Plaza Universitaria from AFICA bond proceeds and/or line of credit and/or any other structure of credit facility; (3) Desarrollos will own the Plaza Universitaria improvements and will lease them exclusively to the UPR, during the life of the AFICA bonds; (4) the UPR shall have the right to prepay or refinance the bonds at any time, consistent with the restrictions on refinancing contained in the financing documents; (5) upon the payment or prepayment in full of all the AFICA bonds, the lease on the land shall terminate and the UPR shall become, *ipso facto*, owner of all the Plaza Universitaria improvements, without the need or obligation to make any additional payment of any kind (other than any bargain purchase payment as may be required under the project documents),

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and (6) rental payments (lease payments) from the UPR shall have a fixed component and a variable component. The fixed component shall be in an amount sufficient to guarantee to bondholders the payment of principal and interest on the AFICA bonds as may be established in the financing documents, and will be pledged to guarantee such payments. The variable component of the lease payments will be used to cover operating, maintenance, administrative, management, and other fees and costs, which will be established periodically and reviewed annually between the parties, as well as such amounts for reserves and special funds, which may be required under the financing documents related to the bond issue.

On December 21, 2000, the UPR entered into a lease agreement with Desarrollos in which the UPR agreed to pay directly to a trustee for the account of Desarrollos, the basic lease payments (denominated into components of principal and interest) on or before the 25th day of each month.

**(g) *PCSDIPRC***

PCSDIPRC provides insurance coverage over the stocks and deposits of all the cooperatives and the Federation of Cooperatives of Puerto Rico. The deposit base of the cooperatives approximates \$5.4 billion at June 30, 2003.

**(h) *LAPR***

LAPR and Sugar Corporation of Puerto Rico, a blended component unit of LAPR, are defendants in various claims amounting to approximately \$104.4 million. LAPR is in the process of litigating such claims but the ultimate outcome cannot presently be determined. Accordingly, no provision for any liability that may result upon a final resolution of such claims has been made in the accompanying basic financial statements. Most of these claims resulted from the closing of several sugar mills throughout the years and from environmental claims.

LAPR has approximately \$44.3 million in accruals to cover the estimated costs related to the liquidation of Sugar Corporation of Puerto Rico including, among others: employee severance, pending legal cases, environmental clean-up costs, refinery repair costs and estimated future losses to be incurred. Management believes these accruals to be sufficient, however given the many uncertainties involved, the ultimate outcome cannot be determined with certainty at this time and the actual liquidation costs could be higher or lower than the estimates made.



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#### *Environmental Commitments and Contingencies*

The following component units' operations include activities that are subject to state and federal environmental regulations:

- **PREPA** – Facilities and operations of PREPA are subject to regulations under numerous federal and Commonwealth environmental laws, including the Clean Air Act, Clean Water Act, and the National Pollutant Discharge Elimination System (NPDES). In February 1992, the U.S. Environmental Protection Agency (EPA) performed an inspection of various facilities of PREPA and became aware of deficiencies in different areas, principally air opacity; water quality; spill prevention control and countermeasures; and underground storage tanks. As a result, PREPA agreed to, among other things, make certain capital improvements, undertake supplemental environmental projects (SEPs), and use fuel oil not exceeding certain predetermined levels of sulfur, vanadium and asphalt in its content.
- **PRASA** – Facilities and operations of PRASA's water and sewer system are subject to regulation under numerous federal and Commonwealth environmental laws. Under agreements with the federal government, acting on behalf of EPA, PRASA and the Commonwealth are subject to consent decrees to enforce compliance with environmental laws. Accordingly, PRASA has assessed stipulated noncompliance penalties. During the year ended June 30, 2003, such penalties amounted to \$2.2 million. In addition, PRASA has committed to perform environmental projects, in lieu of penalties, in the amount of \$2 million as of June 30, 2003.
- **PRSWA** – PRSWA is currently involved in the implementation and development of the Infrastructure Regional Plan for Recycling and Disposal of Solid Waste in Puerto Rico. As of June 30, 2003, PRSWA has no insurance coverage for environmental risks and management believes that, at this time, there is no sufficient information available to determine the potential amount of related losses, if any, and no provision for losses has been made in the PRSWA's financial statements. Nevertheless, preventive infrastructure has been constructed to minimize any possible impact or events that occur. In addition, operational plans have been developed to incorporate good maintenance practices.
- **PRLA** – PRLA was named a potential responsible party along with the Municipality of Juncos and other third parties (collectively the PRPs) for investigation and clean-up costs under federal remediation laws for the contamination of the Juncos Landfill superfund site. On August 21, 2001, the U.S. Department of Justice (DOJ) proposed that the PRPs pay a total of \$5,500,000 in settlement of EPA past cost claims, through November 2000, land penalty and punitive damages claims relating to prior alleged noncompliance. Arrangements are underway to review EPA's cost documentation. While it is not feasible to predict the outcome of such pending investigations and remediation activities with certainty and in view of PRLA's limited involvement with the site, management, after consulting with its legal counsel, is of the opinion that the ultimate outcome of these claims will not have a material effect on PRLA's financial position or results of operations.

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- **PRIDCO** – Financial responsibility for clean-up costs has been and/or is being undertaken by the industrial PRPs at the two Comprehensive Environmental Response Compensation and Liability Act of 1980 (CERCLA) sites (Vega Alta and Guayama), where the federal government named PRIDCO as a PRP solely for being a part-owner of both sites. PRIDCO's participation in the site remediation efforts to date has been limited to providing in-kind support to the industrial PRP's implementation of the clean-up programs and consequently, has not involved any cash disbursements to the federal government or the industrial PRP groups. Under CERCLA and its regulations, liability for the clean-up costs and damage to natural resources and any assessment of health effects may be imposed on the present and past owners or operators of a facility from which there was a release of hazardous substances. In addition, any person who arranged for the disposal or treatment of hazardous substances at a site from which there was a release may also be liable.

#### *Construction Commitments*

As of June 30, 2003, the following component units maintained various unspent construction agreements as follows (expressed in thousands):

Puerto Rico Highway and Transportation Authority	\$	886,770
Special Communities Perpetual Trust		350,000
Puerto Rico Infrastructure Financing Authority		192,000
Puerto Rico Electric Power Authority		183,700
Puerto Rico Convention Center District Authority		108,705
Puerto Rico Aqueduct and Sewer Authority		108,448
University of Puerto Rico		72,245
Puerto Rico Ports Authority		64,305
Puerto Rico Industrial Development Company		57,000
Tourism Company of Puerto Rico		30,375
Puerto Rico Exports Development Corporation		3,763
Puerto Rico Conservatory of Music Corporation		3,287
Puerto Rico Public Broadcasting Corporation		2,819
Fine Arts Center Corporation		1,332

#### (19) Retirement Systems

The Commonwealth sponsors three contributory pension plans (collectively known as the Retirement Systems), which are reported in the accompanying statement of fiduciary net assets:

- Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities
- The Puerto Rico Judiciary Retirement System

## COMMONWEALTH OF PUERTO RICO

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- Puerto Rico System of Annuities and Pensions for Teachers

Each system is independent; thus their assets or liabilities may not be transferred from one system to another or used for any purpose other than to benefit the participants of each system.

The Retirement Systems issue financial reports, which are publicly available and include the basic financial statements, the required trend information, and any other required supplementary information. These reports may be obtained by written request to the corresponding retirement system administrator at the addresses detailed in note one of each retirement system's basic financial statements.

(a) *ERS*

#### Plan Description

The ERS is the administrator of a single-employer (as related to the Commonwealth financial reporting entity) defined-benefit pension plan sponsored by the Commonwealth. ERS was created under Act No. 447 (the Act), approved on May 15, 1951, as amended, and became effective on January 1, 1952. ERS covers substantially all full-time employees of: (1) the Commonwealth's primary government, (2) certain municipalities of Puerto Rico and certain component units of the Commonwealth not having their own retirement systems. Appointed and temporary Commonwealth employees become Plan members upon their date of employment. Plan members are eligible for a retirement annuity upon reaching the following age:

Police and Firemen	Other Employees
50 with 25 years of credited services	55 with 25 years of credited services
58 with 10 years of credited services	58 with 10 years of credited services

Plan members are eligible for merit annuity with a minimum of 30 years or more of credited service.

A participating employee contributes a 5.775% of the monthly salary for the first \$550 and 8.275% for the excess over \$550 on the coordinated plan. By the time the employee reaches 65 years of age and begins to receive social security benefits, the pension benefits are reduced by the following:

- \$165 per month if retired with 55 years of age and 30 years of credited service
- \$110 per month if retired with less than 55 years of age and 30 years of credited service
- All other between \$82 and \$100 per month
- Disability annuities under the coordinated plan are also adjusted at age 65 and in some cases be reduced over \$165 per month.

On the noncoordinated plan the participating employee contributes 8.275% of the monthly salary and does not have any change on the pension benefits upon receipt of social security benefits.

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Death benefits are divided into occupational, nonoccupational and postretirement. Under the occupational benefits a surviving spouse may receive an annuity equal to 50% of the participating employee's salary at the date of death and each child may receive \$10 per month for each child, minor, or student, up to a maximum benefit per family of 100% of the participating employee's salary at the date of death. Under the nonoccupational benefits the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of death are paid. Under the postretirement benefit the beneficiary with surviving spouse age 60 or over and child, 18 or under receive up to 30% of the retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$750.

On September 24, 1999, an amendment to the Act, which created ERS, was enacted to establish a defined contribution plan known as System 2000.

System 2000 became effective on January 1, 2000. Employees participating in the defined-benefit plan system at December 31, 1999, had the option to either stay in the defined-benefit plan or transfer to System 2000. Persons employed on or after January 1, 2000, are only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of plan assets, which will be invested by ERS, together with those of the defined-benefit plan. Benefits at retirement age will not be guaranteed by the Commonwealth. The annuity will be based on a formula which assumes that each year the participants' contributions (with a minimum of 8.275% of the participants' salary up to a maximum of 10%) will be invested as instructed by the participant in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Notes; (2) earn a rate equal to 75% of the return of ERS's investment portfolio (net of management fees); or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The sponsors' contributions (9.275% of the participants' salary) will be used to fund the defined-benefit plan.

System 2000 reduces the retirement age from 65 years to 60 for those employees who joined the original plan on or after January 1, 2000.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

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#### **Funding Policy**

Contribution requirements, which are established by law and are not actuarially determined, are as follows:

Commonwealth and other sponsors	9.275% of applicable payroll
Participants:	
Hired on or before March 31, 1990	5.775% of monthly gross salary up to \$550
	8.275% of monthly gross salary in excess of \$550
Hired on or after April 1, 1990	8.275% of monthly gross salary

#### **(b) JRS**

##### **Plan Description**

The JRS is a single-employer defined-benefit plan, which is also administered by the ERS. The system was created under Act No. 12, approved on October 19, 1954. Membership is made up of all judges of the Judiciary Branch of the Commonwealth.

The system provides retirement as well as death and disability benefits. Benefits vest after 10 years of service and upon reaching 60 years of age.

Retirement benefits are determined by the application of stipulated benefit ratios to the member's average compensation. Average compensation is computed based on the last month of compensation. The retirement annuity, for which the plan participant is eligible, is limited to a minimum of 25% and a maximum of 75% of the average compensation, except for judges of the Supreme Court for whom the annuity is limited to a minimum of 50% and a maximum of 100% of the average compensation.

Death benefits are divided into occupational, nonoccupational and postretirement. Under the occupational benefits a surviving spouse may receive an annuity equal to 50% of the participating employee's salary at the date of death and each child may receive \$10 per month for each child, minor or student, up to a maximum benefit per family of 100% of the participating employee's salary at the date of death. Under the nonoccupational benefits the contributions and interest accumulated as of the date of the death plus an amount equal to the annual compensation at the time of death is paid. Under the postretirement benefit the beneficiary with surviving spouse age 60 or over and child 21 or under receive up to 60% of the retiree's pension or otherwise the excess, if any, of the accumulated contributions at the time of retirement over the total annuity benefits received before death, limited to a minimum of \$500.

During 1997, JRS enacted Act No. 177 which provides, effective January 1, 1999, for increases of 3%, every three years, of the pension benefits paid by JRS to those plan participants with three or more years of retirement.

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#### **Funding Policy**

All participants are required to make contributions to the plan equal to 8% of the applicable payroll. The Commonwealth, as sponsor, must contribute 20% of the applicable payroll. Contributions are established by law and are not actuarially determined.

#### **(c) TRS**

##### **Plan Description**

The TRS is a single-employer defined plan sponsored by the Commonwealth. All active teachers of the Commonwealth's Department of Education are covered by the system under the terms of Act No. 218 of 1951. Licensed teachers working in private schools may also participate in the system as long as the required employer and employee contributions are satisfied.

The plan provides retirement, death, and disability benefits. Benefits vest after completion of a given number of years of credited service based on age. Benefits are determined by the application of stipulated benefit ratios to the members' average compensation. Average compensation is computed based on the highest three years of compensation recognized by TRS.

The annuity for which a plan member is eligible is limited to a minimum of \$300 per month and a maximum of 75% of the average compensation.

##### **Funding Policy**

Effective January 27, 2000, participant contributions were increased to 9% of their compensation, as provided by Act No. 45 of 2000. The Commonwealth, as sponsor, matches the participants' contributions at a rate of 8.5% of the applicable payroll. Contribution rates are established by law, and are not actuarially determined.

Other relevant information on the Commonwealth's Retirement Systems is presented below (as of July 1, 2001, latest valuation date):

#### **Membership**

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>	<u>Total</u>
Retirees and beneficiaries currently receiving benefits	87,648	285	29,213	117,146
Current employees	166,914	338	49,217	216,469
Total	<u>254,562</u>	<u>623</u>	<u>78,430</u>	<u>333,615</u>

# COMMONWEALTH OF PUERTO RICO

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### *Annual Pension Cost and Net Pension Obligation (Asset)*

The Commonwealth's annual pension cost and net pension obligation (asset) of the three pension plans for the year ended June 30, 2003, were as follows (expressed in thousands):

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>	<u>Total</u>
Annual required contributions	\$ 802,536	6,892	172,338	981,766
Interest on net pension obligation (asset)	192,416	(1,430)	28,191	219,177
Adjustment to annual required sponsors' contributions	<u>(134,870)</u>	<u>1,002</u>	<u>(24,292)</u>	<u>(158,160)</u>
Annual pension cost	860,082	6,464	176,237	1,042,783
Statutory sponsors' contributions made	<u>(330,404)</u>	<u>(5,536)</u>	<u>(124,152)</u>	<u>(460,092)</u>
Increase (decrease) in net pension obligation (asset)	529,678	928	52,085	582,691
Net pension obligation (asset) at beginning of year	<u>2,815,576</u>	<u>(15,773)</u>	<u>404,474</u>	<u>3,204,277</u>
Net pension obligation (asset) at end of year	<u>\$ 3,345,254</u>	<u>(14,845)</u>	<u>456,559</u>	<u>3,786,968</u>

The net pension obligation for ERS and TRS, and the net pension asset of JRS of \$3,802 million and \$14.8 million, respectively, are recorded in the accompanying statement of net assets.

The annual required contribution was determined by actuarial valuations for each of the pension plans as described below:

	<u>ERS</u>	<u>JRS</u>	<u>TRS</u>
Date of latest actuarial valuation	July 1, 2001	July 1, 2001	July 1, 2001
Actuarial cost method	Projected unit credit cost	Projected unit credit cost	Entry age normal
Amortization method	Level percentage of the projected payroll	Level percentage of the projected payroll	Level percentage closed 5% payroll increase per year
Remaining amortization period	25 years	25 years	19 years
Amortization approach	Closed	Closed	Closed

# COMMONWEALTH OF PUERTO RICO

## Notes to Basic Financial Statements

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	ERS	JRS	TRS
Asset valuation method	Market value	Market value	Market value
Actuarial assumptions:			
Inflation	3.5%	3.5%	3.5%
Investment rate of return	8.5%	8.5%	8.0%
Projected salary increases per annum	5.0%	5.0%	5.0%
Cost-of-living adjustments	3.0% every three years	3.0% every three years	Not applicable

### Three-Year Trend Information

The three-year trend information is as follows (expressed in thousands):

Annual pension cost (APC)	ERS	JRS	TRS
Year ended June 30, 2003	\$ 860,082	6,464	176,237
Year ended June 30, 2002	860,082	6,464	176,237
Year ended June 30, 2001	803,526	10,052	108,156
Percentage of APC contributed			
Year ended June 30, 2003	38.4%	85.6%	70.4%
Year ended June 30, 2002	35.8%	83.7%	70.4%
Year ended June 30, 2001	65.6%	72.6%	107.3%
Net pension obligation (asset)			
Year ended June 30, 2003	2,815,576	(15,773)	404,474
Year ended June 30, 2002	2,263,722	(16,825)	352,388
Year ended June 30, 2001	2,010,051	(19,250)	378,829

### Schedule of Funding Progress (Required Supplementary Information – Unaudited)

Employees' Retirement System of the Government of Puerto Rico and Its Instrumentalities (expressed in thousands):

Actuarial valuation date	Actuarial value of assets	Actuarial accrued liability (AAL)	Unfunded AAL (UAAL)	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
July 1, 2001	\$ 2,429,000	9,881,000	7,452,000	25%	\$ 2,549,447	292%
July 1, 2000	2,041,800	9,459,300	7,417,500	22%	2,463,400	301%
July 1, 1999	1,858,000	8,308,000	6,450,000	22%	2,275,000	250%



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The Puerto Rico Judiciary Retirement System (expressed in thousands):

Actuarial valuation date	Actuarial value of assets	AAL	UAAL	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
July 1, 2001	\$ 70,100	162,200	92,100	43%	\$ 26,700	345%
July 1, 2000	82,800	135,800	53,000	61%	25,700	206%
July 1, 1999	73,900	118,200	44,300	63%	26,300	168%

Puerto Rico System of Annuities and Pensions for Teachers (expressed in thousands):

Actuarial valuation date	Actuarial value of assets	AAL	UAAL	Funded ratio	Covered payroll	UAAL as a percentage of covered payroll
July 1, 2001	\$ 2,283,000	3,683,000	1,400,000	62%	\$ 871,000	161%
July 1, 2000	2,509,000	3,205,000	696,000	78%	1,006,000	69%
July 1, 1999	2,314,000	2,904,000	590,000	80%	996,000	59%

On August 12, 2000, Act No. 174 was approved to allow certain ERS participants to be eligible for early retirement upon attaining at least age 55 with 25 years of service, provided they made their election on or before April 1, 2001. Those who elected early retirement under this law will receive monthly benefits of 75% (if 25 or more years of service and age 55, or 30 or more years of service and age 50) or benefits of 65% (if 25 years of service by less than age 55) of their average compensation which is computed based on the highest 36 months of compensation recognized by ERS. In these cases, the sponsor is responsible for contributing to ERS amounts to cover the benefit payments and the sponsor contribution with respect to the participants covered until the participants reach the normal retirement age.

## (20) Subsequent Events

### *Primary Government*

On April 30, 2004, the Commonwealth issued \$727 million of General Obligation Bonds consisting of \$279 million of 2004 Series A Public Improvement Refunding Bonds and \$448 million of 2004 Series B Public Improvement Refunding Bonds. The proceeds from these bonds will be used to provide funds to carry out the capital improvement programs authorized by the Commonwealth Legislature, to refund certain General Obligation Bonds of the Commonwealth and to reimburse GDB for advances made to fund subsidies granted to homeowners under Act No. 124 of December 10, 1993. The 2004 Series A Public Improvement Bonds will bear interest rates ranging from 3.83% to 4.2%, payable each July 1 and January 1. The principal is payable each July 1 beginning on July 1, 2004 through July 1, 2032. There are also term bonds of \$279 million due on July 1, 2030 and July 1, 2031, respectively, bearing interest at an annual interest rate ranging between 4% and 5%.

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On November 13, 2003, the Commonwealth issued \$234 million 2003 B Series Public Improvement Refunding Bonds. These bonds bear interest ranging from 1.5% to 5% and are due on July 1, 2004 through 2014. Term Bonds from 2019 to 2033 bear interest ranging from 5.50% to 5.694%.

On October 3, 2003, the Commonwealth issued \$457 million in 2004 Series A Public Improvement Bonds. These bonds will bear interest ranging from 2% to 5.25%, and term bonds at 5% due between July 1, 2027 and July 1, 2033.

On October 3, 2003, the Commonwealth issued \$800 million tax and revenue anticipation notes for the purpose of funding a portion of the projected cash flow requirements of the general fund in fiscal year 2004, which requirements result from timing differences between expected disbursements and receipts of taxes and other revenue. The notes are due on July 30, 2004, and bear an annual interest rate ranging from 2% to 3.5%.

On May 12, 2004, the PBA, a blended component unit of the Commonwealth, issued \$832,385,000 Government Facilities Revenue Refunding Bond Series I, and \$335,580,000 Government Facilities Revenue Bonds Series J. The proceeds from the Series I Bonds will be used (1) to pay a portion of the costs of construction of certain buildings and facilities to be leased by PBA to various departments and instrumentalities of the Commonwealth, (2) repay a portion of certain advances made to PBA by GDB under a line-of-credit facility, (3) to pay capitalized interest, and (4) to pay cost of issuance of Series I Bonds. The proceeds of Series J Bonds will be used (1) for the purpose of refunding certain bonds issued under the 1995 Bond Resolutions, (2) for the purpose of refunding interest (but not principal) on certain bonds issued under the 1995 Bond Resolutions, and (3) to pay cost of issuance of Series J Bonds. The Facilities Revenue Bonds Series I and the Series J will bear fixed interest rates ranging from 5.37% to 5.50% payable semiannually on each July 1 and January 1 of each year, beginning on July 1, 2004 through July 1, 2036.

On May 27, 2004, the PBA, a blended component unit of the Commonwealth, issued \$347,065,000 Government Facilities Revenue Refunding Bond Series K, and \$6,795,000 Government Facilities Revenue Bonds Series L. The proceeds of Series K Bonds will be used (1) for the purpose of refunding certain bonds issued under the 1995 Bond Resolutions, (2) for the purpose of refunding interest (but not principal) on certain bonds issued under the 1995 Bond Resolutions, and (3) to pay cost of issuance of Series K Bonds. The proceeds of Series L Bonds will be used to (1) pay the interest that has accrued under a line of credit with GDB used by PBA to defray a portion of the costs of construction of certain government facilities leased by PBA to departments, agencies, instrumentalities, and municipalities of the Commonwealth, and (3) to pay cost of issuance of Series L Bonds. The Facilities Revenue Bonds Series K and the Series L will bear fixed interest rates ranging from 3.60% to 4.50% payable semiannually on each July 1 and January 1 of each year, beginning on January 1, 2005 through July 1, 2027.

During December 2003, HUD approved, subject to certain conditions a financing arrangement with PHA amounting to approximately \$693 million for the modernization of approximately 40 properties containing approximately 8,000 units. This bond financing program is part of an overall PHA's accelerated modernization program for 111 properties, containing approximately 20,830 units. A total of 53 of the 111

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properties, totaling 8,654 housing units, are already under a construction contract and all or portions of the work relative to these projects have been completed.

#### *Component Units*

##### *(a) GDB*

On August 6, 2003, the Tourism Development Fund initiated foreclosure on the mortgage note it holds as collateral for the guarantee on the AFICA Cayo Largo bonds. The indenture of the AFICA Cayo Largo Bonds requires the repayment of the bonds before the execution of the mortgage note. Therefore, in order to execute the mortgage note, the Tourism Development Fund obtained a line of credit from GDB just prior to filing the foreclosure action, with which the Tourism Fund called the outstanding balance of the AFICA Cayo Largo bonds. Said bonds amounted to \$75.6 million.

In July 2003, the Tourism Development Fund, a blended component unit of GDB, obtained a line of credit from GDB for a maximum of \$155.3 million with the sole purpose of refinancing the AFICA Río Mar Associates bonds which the Tourism Fund guarantees. Said bonds have an outstanding balance of \$148.8 million at June 30, 2003.

In July 2003, the PFC issued approximately \$382 million of Commonwealth Appropriations Bonds maturing at various dates through 2025. The proceeds of the bonds, except for their related cost of issuance, were used to refund a debt recorded as loans from the public sector by GDB from the Land Authority, according to Act No. 164 of December 17, 2001 and the PRMSA and Property Tax Settlement Commonwealth Appropriation Bonds discussed in note 14(d).

##### *(b) PRHTA*

On October 30, 2003, PRHTA issued Special Facility Revenue Refunding Bonds, 2003 Series A amounting to approximately \$153 million for the purpose of refunding the PRHTA's Special Facility Revenue Bonds, 1992 Series A, B, and C, which were issued to fund the construction of the Teodoro Moscoso Bridge, and to pay the cost of issuance of the bonds. The proceeds from the sale of the bonds were transferred by PRHTA to Autopistas de Puerto Rico, pursuant to a new loan agreement by and between Autopistas de Puerto Rico and PRHTA.

##### *(c) PREPA*

On July 2, 2003, PREPA and GDB entered into a \$68 million line-of-credit agreement to finance a settlement agreement relating to certain litigation with the municipalities of Puerto Rico.

On August 8, 2003, PREPA issued \$517,305,000 Power Revenue Bonds, Series NN to finance a portion of the cost of various projects under its capital improvement program.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

On August 18, 2003, the Commonwealth approved Act No. 189 which authorizes PREPA to create, acquire, and maintain corporations, partnerships or subsidiary corporations, profit or nonprofit entities.

#### *(d) PRASA*

From May 1995 until March 2004, the operation, management, repair, and maintenance of PRASA's systems were in the hands of private companies. The most recent agreement for the private management of PRASA's systems was entered into in May 2002. However, in January 2004 PRASA and the private operator agreed to terminate their agreement and in April 2004, the operation, management, repair, and maintenance of the PRASA systems returned to PRASA. As part of the plan for the return of the operation and management of the PRASA systems to PRASA, legislation was enacted in March 2004 to restructure PRASA and provide further powers to improve its operational and financial management. The main areas of this restructuring included (1) decentralizing the administration of PRASA, (2) creating five new positions which will manage each region and manage capital improvement projects; and (3) providing for six-year appointments for each of the key executives aiming to give continuity to top management in order to better implement, supervise, and revise as needed the 10-year plan and goals identified for PRASA in 2002 and included in the management contract with the private operator. Further powers granted include the authority to make certain determinations and take certain actions with respect to compliance of the water and sewer system with various federal environmental laws.

As part of the termination agreement, PRASA and the private operator entered into an agreement pursuant to which the parties agreed to settle certain outstanding and potential claims in connection with the service agreement and terminate mutually release each other in respect of certain of their rights and obligations. The settlement results in a net balance due to PRASA of approximately \$3.4 million.

On September 17, 2003, an issuance of Rural Development Bonds, Series CC for \$43.7 million was made at 4.5% of interest, payable semiannually and maturing on 2043. The funds raised by this issuance will pay certain lines of credit which funded several development projects. The payment of principal and interest on this issuance is guaranteed by the Commonwealth.

For fiscal year ending June 30, 2004, the Commonwealth did not budget or provide the \$35 million subsidy appropriation, as approved by the Puerto Rico Legislature on August 1, 1997.

#### *(e) SIFC*

In November 2003, SIFC entered into an interagency agreement with PRSWA for the sale of certain land and property classified as capital asset held for sale. The agreement has been authorized by the Commonwealth's legislative branch and will be financed through a credit facility to be provided by GDB. Among significant terms of the sale agreement, the expected selling price will be \$56 million plus reimbursement of certain expenses being incurred by SIFC since August 2002, related to the maintenance and insurance of the property. Also, the agreement calls for an escrow account of \$3.5

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

million to be retained by the purchaser to cover for any hidden construction faults, if any, during the inspection and transfer of ownership period. SIFC's management believes that no cost will be incurred regarding the inspection of the building as the contractor provided assurance to bear any cost, if applicable.

*(f) PRIDCO*

During the month of July 2003, PRIDCO issued \$135.8 million of General Purpose Revenue Bonds Series 2003 and \$25.9 million of Refunding Revenue Bonds Series 2003. The General Purpose Revenue Bonds Series 2003 were issued to provide funds for the repayment of PRIDCO's line of credit for capital improvements with GDB, to deposit \$2.7 million in the Bond Service Account, and to finance additional industrial facilities. The Refunding Revenue Bonds Series 2003 were issued to refund \$10.7 million aggregate principal amount of General Purpose Revenue Bonds Series 1991 and \$14.7 million aggregate accreted value of Refunding Revenue Bonds Series 1991.

*(g) AFICA*

On August 21, 2003, AFICA declared the coliseum project's main contractor to be in default with the construction contract and required the payment and performance bond provider to assume its obligations under the performance bond. The declaration of default was triggered primarily by continuous delays and postponement of the completion date of the project and the main contractor's failure to pay subcontractors and suppliers, among other things. The main contractor was then required to vacate the project premises and AFICA assumed its control and security. AFICA is undergoing negotiations with the parties involved, including the bond company, the main contractor and subcontractors in order to resume construction activity. In connection with these events, and upon notification that the main contractor had failed to maintain property insurance on the coliseum, AFICA obtained property insurance on the project at a cost of \$1 billion, which became effective on August 29, 2003.

*(h) TCPR*

On September 9, 2003, Act No. 272 was approved transferring the imposition and collection of hotel room taxes pursuant to Sections 2051 and 2084 of the 1994 Puerto Rico Internal Revenue Code and the related responsibilities of administering, supervising, and regulating such tax imposition and collection from the Department of the Treasury of the Commonwealth to the TCPR. Act No. 272 also redefined the formula for the distribution of the hotel room tax proceeds.

This law becomes effective 180 days after its approval date, except for the redefined distribution formula which becomes effective retroactive to July 1, 2003.

## COMMONWEALTH OF PUERTO RICO

### Notes to Basic Financial Statements

June 30, 2003

*(i) SCPT*

Through March 2004, the board of directors of SCPT has approved special communities development projects in the amount of \$976 million of which \$72 million have been incurred.

*(j) PRSWA*

On November 21, 2003, PRSWA signed a purchase agreement with SIFC for the acquisition of land and building in the amount of \$56 million, funds to be paid from the proceeds of a line of credit in the amount of \$75 million with GDB. This will allow the centralization of agencies related to the environment, such as the Solid Waste Authority, the Department of Natural Resources, the Energy Office, and the Environmental Quality Board.

**COMBINING, INDIVIDUAL FUND  
FINANCIAL STATEMENTS AND SCHEDULES**

## **GENERAL FUND**

The general fund is the primary operating fund of the Commonwealth. The general fund is used to account for resources traditionally associated with government, which are not required legally or by sound financial management to be accounted for in another fund. Included are transactions for services such as general government, public safety, health, public housing and welfare, education, and economic development. Following is the supplemental schedule of expenditures – budget and actual – general fund.



# COMMONWEALTH OF PUERTO RICO

## Supplemental Schedule of Expenditures by Agency – Budget and Actual – Statutory Basis – General Fund

Year ended June 30, 2003  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
Expenditures:				
Current:				
General government:				
Senate of Puerto Rico	\$ 33,282	32,539	31,130	1,409
House of Representatives of Puerto Rico	39,500	40,513	40,325	188
Comptroller's Office	34,081	34,201	33,765	436
Governor's Office	12,085	6,541	6,559	(18)
Office of Management and Budget	88,494	28,145	29,092	(947)
Planning Board	10,999	11,740	11,590	150
Constructions and Land Subdivisions Appeals Board	1,425	1,344	1,343	1
Department of State	11,031	11,403	9,873	1,530
Department of the Treasury	163,837	163,837	176,408	(12,571)
Central Office of Personnel Administration	6,197	6,557	6,494	63
Commonwealth Elections Commission	29,665	30,751	30,783	(32)
Federal Affairs Administration	9,245	9,352	9,052	300
General Services Administration	1,670	2,188	1,701	487
Municipal Complaints Hearing Commission	4,276	4,313	4,116	197
Civil Rights Commission	991	978	1,028	(50)
Office of the Citizen's Ombudsman	3,554	3,634	3,626	8
Rules and Permits Administration	1,000	988	988	—
Commonwealth's Commission to Settle Municipal Complaints	197	190	190	—
Legislative Affairs Office	775	775	401	374
Commission for the Public Service Work Relations	1,985	2,049	2,049	—
Central Communications Office	1,808	4,939	4,890	49
Government Ethics Board	7,872	8,066	8,066	—
Legislative Affairs Office	9,735	8,256	7,661	595
Office of the Superintendent of the Capitol	6,444	7,339	7,509	(170)
Comptroller's Special Reports Joint Commission	634	602	602	—
Legislative Donation Commission	700	619	147	472
Coordination Office for Special Communities of Puerto Rico	—	498	482	16
Public Affairs	—	1,676	1,660	16
Governor's Secretary Office	—	11,294	11,295	(1)
Total general government	<u>481,482</u>	<u>435,327</u>	<u>442,825</u>	<u>(7,498)</u>
Public safety:				
Puerto Rico General Court of Justice	217,583	224,434	226,101	(1,667)
State Civil Defense Agency	—	2	232	(230)
Commission of Investigation, Processing, and Appeals Board	676	699	699	—
Department of Justice	127,486	125,011	113,528	11,483
Puerto Rico Police Department	625,111	631,498	611,666	19,832
Puerto Rico Firefighters Corps.	46,934	48,752	48,748	4
Puerto Rico National Guard	7,911	7,847	7,835	12
Public Service Commission	9,020	9,559	9,559	—
Consumer Affairs Department	12,351	12,459	12,306	153
Juvenile Institutions Administration	86,328	81,833	82,932	(1,099)
Corrections Administration	336,485	337,335	370,489	(33,154)
Department of Correction and Rehabilitation	3,870	4,005	4,001	4
Natural Resources Administration	26,855	33,502	34,688	(1,186)
Balance carried forward	<u>\$ 1,500,610</u>	<u>1,516,936</u>	<u>1,522,784</u>	<u>(5,848)</u>

**COMMONWEALTH OF PUERTO RICO**

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2003  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
Balance brought forward	\$ 1,500,610	1,516,936	1,522,784	(5,848)
Parole Board	3,079	3,046	3,046	—
Forensic Sciences Institute	8,506	9,360	9,360	—
Special Prosecutor Panel	1,917	1,951	1,951	—
Pre-Trial Services Office	3,710	4,035	4,042	(7)
Correctional Health	77,993	78,818	78,821	(3)
Medical Emergencies Service	15,992	17,198	17,183	15
Total public safety	<u>1,611,807</u>	<u>1,631,344</u>	<u>1,637,187</u>	<u>(5,843)</u>
Health:				
Environmental Quality Board	7,565	8,046	8,111	(65)
Department of Health	177,576	150,626	174,120	(23,494)
Mental Health and Drug Addiction Services Administration	94,475	103,942	101,308	2,634
Drug Control	1,629	1,256	1,455	(199)
Pediatric University Hospital	14,500	14,500	14,483	17
Solid Waste Authority of Puerto Rico	6,200	6,430	7,430	(1,000)
Puerto Rico Health Insurance Administration	883,601	885,896	892,984	(7,088)
Total health	<u>1,185,546</u>	<u>1,170,696</u>	<u>1,199,891</u>	<u>(29,195)</u>
Public housing and welfare:				
Rural Housing Administration	7,549	8,107	8,103	4
Puerto Rico Volunteers Service Corps.	10,916	11,473	11,472	1
Department of Labor and Human Resources	6,351	6,497	6,495	2
Labor Relations Board	1,280	1,314	1,330	(16)
Department of Housing	7,894	8,332	31,799	(23,467)
Department of Recreation and Sports	37,908	38,941	41,897	(2,956)
Administration for the Horse Racing Sport and Industry	3,087	3,187	3,166	21
Women's Affairs Commission	5,353	5,404	2,744	2,660
Public Housing Administration	1,272	1,364	1,358	6
Office of the Veteran's Ombudsman	1,154	1,190	1,185	5
Department of Family	33,264	35,667	35,272	395
Family and Children Administration	115,248	117,505	116,477	1,028
Child Support Administration	8,466	9,397	9,339	58
Vocational Rehabilitation Administration	17,164	17,655	17,655	—
Social Economic Development Administration	74,008	75,965	104,576	(28,611)
Office of the Disabled Persons Ombudsman	2,312	2,417	2,421	(4)
Office for Elderly Affairs	3,319	3,431	3,231	200
Communities Rehabilitation Administration	4,368	4,933	4,646	287
Patient Ombusman	4,183	4,527	4,554	(27)
Office of the General Auditor – Department of Family	512	397	399	(2)
Institutional Trust of the National Guard of Puerto Rico	495	495	495	—
Right to Employment Administration	9,463	9,909	9,909	—
Cantera's Peninsula Integral Development Company	742	192	192	—
Puerto Rico Housing Finance Authority	—	550	550	—
Industries for the Blind, Mentally Retarded, and Other Disabled Persons of Puerto Rico	141	141	141	—
Total public housing and welfare	<u>\$ 356,449</u>	<u>368,990</u>	<u>419,406</u>	<u>(50,416)</u>

**COMMONWEALTH OF PUERTO RICO**

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2003  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
Education:				
Department of Education	\$ 1,700,541	1,691,271	1,741,357	(50,086)
State Office for Historic Preservation	1,757	1,775	3,692	(1,917)
General Education Council	1,724	1,765	1,767	(2)
Athenaeum of Puerto Rico	360	360	360	—
Institute of Puerto Rico Culture	25,818	27,027	26,892	135
Plastic Arts School	2,432	2,519	2,512	7
University of Puerto Rico	687,102	687,204	687,202	2
Musical Arts Corporation	6,360	6,411	6,411	—
Fine Arts Center Corporation	2,604	2,754	2,754	—
Puerto Rico Public Broadcasting Corporation	21,421	21,916	21,916	—
Puerto Rico Conservatory of Music Corporation	3,434	3,560	3,560	—
Puerto Rico Higher Education Council	17,554	17,650	17,650	—
Institute of Linguistic Planification	1,000	1,000	—	1,000
Total education	<u>2,472,107</u>	<u>2,465,212</u>	<u>2,516,073</u>	<u>(50,861)</u>
Economic development:				
Department of Transportation and Public Works	57,476	58,564	74,907	(16,343)
Department of Natural and Environmental Resources	739	940	930	10
Department of Agriculture	18,265	21,247	20,752	495
Department of Economic Development and Commerce	9,605	9,730	10,822	(1,092)
Cooperative Enterprises Development Administration	2,949	3,049	3,212	(163)
Cooperative Enterprises Inspector's Office	895	922	922	—
Rural Development Corporation	2,263	2,468	2,463	5
Department of Economic Development and Commerce	3,241	2,982	3,003	(21)
Energy Affairs Administration	161	137	135	2
Culebra Conservation and Development Authority	401	433	433	—
Corporation for the Development of the Film Industry in Puerto Rico	1,334	1,035	1,036	(1)
Agricultural Extension Services	2	2	2	—
Puerto Rico Infrastructure Financing Agency	70,590	74,290	74,290	—
Puerto Rico Aqueduct and Sewer Authority	184,360	184,360	187,774	(3,414)
Puerto Rico Industrial Development Company	15,333	15,333	25,333	(10,000)
Puerto Rico Electric Power Authority	—	20	6,071	(6,051)
Puerto Rico Metropolitan Bus Authority	479	479	479	—
Puerto Rico Maritime Transportation Authority	15,500	15,500	15,500	—
Tourism Company of Puerto Rico	7,021	7,021	7,021	—
Agricultural Services and Development Administration	91,723	89,584	89,584	—
National Parks Company of Puerto Rico	14,338	14,671	31,764	(17,093)
Corporation for the Development of the Film Industry in Puerto Rico	1,007	1,014	1,011	3
Puerto Rico Land Administration	2,388	2,388	2,388	—
Sugar Corporation	—	6,160	6,160	—
Port of the Americas Authority	9,860	—	—	—
Total economic development	<u>509,930</u>	<u>512,329</u>	<u>565,992</u>	<u>(53,663)</u>
Intergovernmental:				
Vieques Commissioner's Office	1,175	983	1,306	(323)
Appelative Board of the Personnel System Administration	1,429	1,471	1,474	(3)
Municipal Service Administration	344,296	347,800	358,600	(10,800)
Total intergovernmental	<u>\$ 346,900</u>	<u>350,254</u>	<u>361,380</u>	<u>(11,126)</u>

**COMMONWEALTH OF PUERTO RICO**

Supplemental Schedule of Expenditures by Agency – Budget and Actual –  
Statutory Basis – General Fund

Year ended June 30, 2003  
(In thousands)

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance</u>
Debt service:				
Principal	\$ 69,740	69,740	69,740	—
Interest and other	153,333	153,333	153,333	—
Total expenditures	<u>223,073</u>	<u>223,073</u>	<u>223,073</u>	<u>—</u>
Other financing uses:				
Transfer out to other funds:				
Senate of Puerto Rico	—	(1,453)	(1,453)	—
House of Representatives of Puerto Rico	—	(33)	(33)	—
Comptroller's Office	—	(863)	(863)	—
Puerto Rico General Court of Justice	—	(558)	(558)	—
Office of Youth Affairs	(3,027)	(3,128)	(3,116)	(12)
Office of Management and Budget	(193,431)	(193,431)	(193,431)	—
Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities	(104,060)	(109,120)	(109,051)	(69)
Rural Housing Administration	—	—	(17)	17
Civil Rights Commission	—	(52)	(52)	—
Office of the Citizen's Ombudsman	—	(42)	(42)	—
Department of Health	—	(8,000)	(8,000)	—
Teachers' Pensions Board	(15,353)	(27,490)	(27,490)	—
Contributions to Political Parties	(900)	(900)	(900)	—
Legislative Affairs Office	—	(1,637)	(1,637)	—
Department of Housing	—	—	(1,500)	1,500
Comptroller's Special Reports Joint Commission	—	(32)	(32)	—
Legislative Donation Commission	—	(101)	(101)	—
Department of Treasury – Transfer to debt service	(331,935)	(331,935)	(331,935)	—
Transfer in from component units	<u>282,000</u>	<u>282,000</u>	<u>263,586</u>	<u>18,414</u>
Total tranfers out to other funds	<u>\$ (366,706)</u>	<u>(396,775)</u>	<u>(416,625)</u>	<u>19,850</u>

## NONMAJOR GOVERNMENTAL FUNDS

### *Special Revenue Funds*

Special revenue funds are used to account for the proceeds of specific revenue sources that are legally restricted to expenditure for specific purposes.

**Public Building Authority Special Revenue Fund:** The operating fund of a blended component unit used to account for the operation, maintenance, equipment replacement, and other extraordinary operation and maintenance costs of the buildings and facilities that, when constructed, are leased to the Commonwealth's primary government agencies.

### *Debt Service Funds*

The debt service funds are used to account for the accumulation of resources predominantly for, and the payment of, general long-term bonds principal, interest, and related costs other than bonds payable from operations of proprietary fund types, pension trust funds, and discretely presented component units. Long-term debt and interest due on July 1 of the following year are accounted as a fund liability if resources are available as of June 30 for its payment.

**Public Buildings Authority Debt Service Fund:** A blended component unit engaged in the construction and/or acquisition of building facilities for lease mainly to the Commonwealth's primary government agencies. Its debt service fund is used to account for the accumulation of resources for the payment of revenue bonds and other liabilities incurred to finance the construction of the buildings and facilities.

**Puerto Rico Maritime Shipping Authority Debt Service Fund:** This is the remainder of a former shipping company owned by the Commonwealth. Its debt service fund is used to account for the accumulation of resources for the payment of the long-term liability that resulted from the sale of its marine operations. This fund is mainly subsidized from appropriations and operating transfers from the general fund.

**The Children's Trust Debt Service Fund:** The debt service fund of The Children's Trust (a blended component unit) accounts for the accumulation of resources for payment of interest and principal on long-term obligations financed with moneys to be received by the Commonwealth from the global settlement agreement signed by certain tobacco companies.

### *Capital Project Funds*

Capital project funds are used to account for the financial resources used for the acquisition or construction of major capital facilities not being financed by proprietary fund types, pension trust funds, and discretely presented component units.

**Commonwealth Public Improvements Funds and Other Funds:** These funds present the activities of the capital improvements program of the Commonwealth, financed with the proceeds of the general obligation bonds.

# COMMONWEALTH OF PUERTO RICO

Combining Balance Sheet — Nonmajor Governmental Funds

June 30, 2003  
(In thousands)

	Special revenue		Debt service			Capital projects		Total nonmajor governmental funds
	Public Building Authority	Public Building Authority	Puerto Rico Maritime Shipping Authority	The Children's Trust	Total	Commonwealth of Puerto Rico		
Assets								
Cash and cash equivalents	\$ 6,764	—	—	—	—	16,464	23,228	
Cash and cash equivalents in governmental banks	12,350	—	2,398	—	2,398	375,868	390,616	
Investments	5,218	—	594	115,337	115,931	—	121,149	
Receivables, net of allowance for uncollectibles:								
Accounts	14,846	—	—	—	—	671	15,517	
Loans	—	—	—	—	—	36	36	
Due from:								
Other funds	13,653	39,010	—	—	39,010	30,371	83,034	
Component units	25,597	—	—	—	—	—	25,597	
Restricted assets:								
Cash and cash equivalents	725	6,054	—	—	6,054	—	6,779	
Cash and cash equivalents in governmental banks	4,089	90,877	—	—	90,877	—	94,966	
Total assets	\$ 83,242	135,941	2,992	115,337	254,270	423,410	760,922	
Liabilities and Fund Balances								
Liabilities:								
Accounts payable and accrued liabilities	\$ 43,338	—	1,305	—	1,305	7,881	52,524	
Bonds payable	—	42,315	—	—	42,315	—	42,315	
Interest payable	—	48,402	—	—	48,402	—	48,402	
Other liabilities	5,000	—	—	—	—	11,424	16,424	
Total liabilities	48,338	90,717	1,305	—	92,022	19,305	159,665	
Fund balances:								
Reserved for encumbrances	—	—	—	—	—	33,047	33,047	
Unreserved reported in:								
Special revenue funds	34,904	—	—	—	—	—	34,904	
Debt service funds	—	45,224	1,687	115,337	162,248	—	162,248	
Capital projects funds	—	—	—	—	—	371,058	371,058	
Total fund balances	34,904	45,224	1,687	115,337	162,248	404,105	601,257	
Total liabilities and fund balances	\$ 83,242	135,941	2,992	115,337	254,270	423,410	760,922	

# COMMONWEALTH OF PUERTO RICO

Combining Statement of Revenue, Expenditures, and Changes in  
Fund Balances – Nonmajor Governmental Funds

Year ended June 30, 2003  
(In thousands)

	Special revenue		Debt service			Capital projects		Total nonmajor governmental funds
	Public Building Authority	The Children's Trust	Public Building Authority	Puerto Rico Maritime Shipping Authority	Commonwealth of Puerto Rico	Total		
Revenue:								
Revenue from global tobacco settlement agreement	—	101,849	—	—	—	101,849	—	101,849
Interest and investment earnings	3,268	1,111	—	94	—	1,205	—	4,473
Other	—	—	—	143	—	143	172	315
Total revenue	3,268	102,960	—	237	—	103,197	172	106,637
Expenditures:								
Current:								
General government	129,068	—	—	—	—	—	249,027	378,095
Intergovernmental	—	—	—	—	—	—	57,759	57,759
Capital outlays	—	—	—	—	—	—	192,384	192,384
Debt service:								
Principal	—	21,120	58,006	6,770	—	85,896	—	85,896
Interest and other	—	48,834	76,576	17,435	—	142,845	—	142,845
Debt issuance costs	—	—	647	—	—	647	10,948	11,595
Payment to escrow agent	—	440,828	—	—	—	440,828	—	440,828
Total expenditures	129,068	69,954	135,229	24,205	—	229,388	510,118	868,574
Excess (deficiency) of revenue over (under) expenditures	(125,800)	33,006	(135,229)	(23,968)	—	(126,191)	(509,946)	(761,937)
Other financing sources (uses):								
Transfers from other funds	113,204	544,825	115,414	24,205	—	684,444	—	797,648
Transfers to other funds	—	(61,388)	—	—	—	(61,388)	(27,797)	(89,185)
Debt issued	—	—	—	—	—	—	563,676	563,676
Refunding bond issues	—	—	439,195	—	—	439,195	—	439,195
Payment to escrow agent	—	(440,828)	(439,195)	—	—	(880,023)	—	(880,023)
Total other financing sources (uses)	113,204	42,609	115,414	24,205	—	182,228	535,879	831,311
Excess (deficiency) of revenue and other financing sources over (under) expenditures and other financing uses	(12,596)	75,615	(19,815)	237	—	56,037	25,933	69,374
Fund balances, beginning of year (as restated)	47,500	39,722	65,039	1,450	—	106,211	378,172	531,883
Fund balances, end of year	34,904	115,337	45,224	1,687	—	162,248	404,105	601,257

## NONMAJOR PROPRIETARY FUNDS

Proprietary funds are used to account for operations that are financed and operated in a manner similar to private business enterprises where the intent of the government is that the costs of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

**Puerto Rico Water Pollution Control Revolving Fund:** It was created by Act No. 44 on June 21, 1988, as amended. It is administered, pursuant to Act No. 9 of June 18, 1970, as amended, by the Puerto Rico Environmental Quality Board (EQB). Pursuant to such Act, EQB is authorized to enter into operating and capitalization grant agreements with the U.S. Environmental Protection Agency (EPA) for lending activities.

**Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund:** It was created by Act No. 32. It is administered pursuant to Act No. 9 of June 18, 1970, as amended, by the Puerto Rico Department of Health (DOH). Pursuant to such act, DOH, on behalf of the Commonwealth, is authorized to enter into operating and capitalization grant agreements with the U.S. Environmental Protection Agency (EPA) for lending activities.

**Disability Insurance:** It was created by Act No. 139 on June 26, 1968. It is used to account for disability benefits to remedy temporarily the loss of income as a consequence of disability caused by sickness or accident unrelated to the employment.

**Drivers' Insurance:** It was created by Act No. 428 on May 15, 1950. It is used to account for contributions made by the drivers and their employers to provide a social security plan for the benefit of the drivers in Puerto Rico. The plan also includes payment of benefits for health and life insurance.





**COMMONWEALTH OF PUERTO RICO**

Combining Statement of Net Assets –  
Nonmajor Proprietary Funds

June 30, 2003  
(In thousands)

<b>Business-type activities – nonmajor enterprise funds</b>					
	<b>Disability insurance</b>	<b>Drivers' insurance</b>	<b>Puerto Rico Water Control Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
<b>Assets</b>					
Current assets:					
Cash and cash equivalents	\$ 64,445	35,740	29,759	11,602	141,546
Accounts and loans receivable, net:					
Insurance premiums, net	3,516	1,061	—	—	4,577
Component units	—	—	9,042	—	9,042
Accrued interests	420	10	1,141	229	1,800
Other	239	26	133	—	398
Restricted investments	36,024	—	—	—	36,024
Total current assets	104,644	36,837	40,075	11,831	193,387
Noncurrent assets:					
Loans receivable, excluding current portion, net:					
Component units	—	—	105,705	23,681	129,386
Intergovernmental	—	—	1,940	—	1,940
Total assets	104,644	36,837	147,720	35,512	324,713
<b>Liabilities and Net Assets</b>					
Current liabilities:					
Accounts payable and accrued liabilities	324	136	512	74	1,046
Deferred revenue	—	30	—	—	30
Compensated absences	356	256	—	—	612
Disability and drivers' insurance benefits	912	203	—	—	1,115
Total current liabilities	1,592	625	512	74	2,803
Noncurrent liabilities – compensated absences	265	219	—	—	484
Total liabilities	1,857	844	512	74	3,287
Net assets:					
Restricted for:					
Disability and drivers' insurance benefits	102,787	35,993	—	—	138,780
Capital projects	—	—	147,208	35,438	182,646
Total net assets	\$ 102,787	35,993	147,208	35,438	321,426

**COMMONWEALTH OF PUERTO RICO**

Combining Statement of Revenue, Expenditures, and Changes in Net Assets  
Nonmajor Proprietary Funds

Year ended June 30, 2003  
(In thousands)

	<b>Business-type activities – nonmajor enterprise funds</b>				
	<b>Disability insurance</b>	<b>Drivers' insurance</b>	<b>Puerto Rico Water Control Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
Operating revenue:					
Insurance premiums	\$ 14,936	4,818	—	—	19,754
Interest	1,964	193	2,425	495	5,077
Total operating revenue	<u>16,900</u>	<u>5,011</u>	<u>2,425</u>	<u>495</u>	<u>24,831</u>
Operating expenses:					
Disability and drivers' insurance benefits	4,216	1,313	—	—	5,529
General, administrative, and other operating expenses	<u>12,773</u>	<u>2,705</u>	<u>491</u>	<u>887</u>	<u>16,856</u>
Total operating expenses	<u>16,989</u>	<u>4,018</u>	<u>491</u>	<u>887</u>	<u>22,385</u>
Operating income (loss)	<u>(89)</u>	<u>993</u>	<u>1,934</u>	<u>(392)</u>	<u>2,446</u>
Nonoperating revenue:					
Contributions from federal government	—	—	9,598	5,480	15,078
Contributions from component units	—	—	—	1,038	1,038
Interest and investment earnings	<u>1,526</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>1,526</u>
Total nonoperating revenue	<u>1,526</u>	<u>—</u>	<u>9,598</u>	<u>6,518</u>	<u>17,642</u>
Income before transfers	1,437	993	11,532	6,126	20,088
Transfers from general fund	<u>—</u>	<u>—</u>	<u>1,742</u>	<u>—</u>	<u>1,742</u>
Change in net assets	1,437	993	13,274	6,126	21,830
Net assets, beginning of year	<u>101,350</u>	<u>35,000</u>	<u>133,934</u>	<u>29,312</u>	<u>299,596</u>
Net assets, end of year	<u>\$ 102,787</u>	<u>35,993</u>	<u>147,208</u>	<u>35,438</u>	<u>321,426</u>

**COMMONWEALTH OF PUERTO RICO**

Combining Statement of Cash Flows –  
Nonmajor Proprietary Funds

Year ended June 30, 2003  
(In thousands)

	<b>Business-type activities – nonmajor enterprise funds</b>				
	<b>Disability insurance</b>	<b>Drivers' insurance</b>	<b>Puerto Rico Water Control Pollution Revolving Fund</b>	<b>Puerto Rico Safe Drinking Water Treatment Revolving Loan Fund</b>	<b>Total nonmajor enterprise funds</b>
Cash flows from operating activities:					
Receipts from customers and users	\$ 14,827	4,776	—	—	19,603
Payments to suppliers and employees	(13,613)	(2,664)	—	—	(16,277)
Payments of disability and drivers' insurance benefits	(4,186)	(1,187)	—	—	(5,373)
Management fees paid	—	—	15	(849)	(834)
Net cash (used in) provided by operating activities	(2,972)	925	15	(849)	(2,881)
Cash flows from noncapital financing activities:					
Intergovernmental grants and contributions	—	—	9,598	5,359	14,957
Operating transfers in from general fund	—	—	1,741	1,159	2,900
Net cash provided by noncapital financing activities	—	—	11,339	6,518	17,857
Cash flows from investing activities:					
Interests received on deposits and investments	1,998	208	4,378	456	7,040
Principal collected on loans	—	—	10,961	—	10,961
Loans originated	—	—	(11,491)	(5,669)	(17,160)
Net cash provided by (used in) investing activities	1,998	208	3,848	(5,213)	841
Net increase (decrease) in cash and cash equivalents	(974)	1,133	15,202	456	15,817
Cash and cash equivalents, beginning of year	65,419	34,607	14,557	11,146	125,729
Cash and cash equivalents, end of year	\$ 64,445	35,740	29,759	11,602	141,546
Reconciliation of operating income to net cash provided by (used in) operating activities:					
Operating income (loss)	\$ (89)	993	1,934	(392)	2,446
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:					
Increase in accounts and loans receivable	(108)	(42)	(2,426)	(6,125)	(8,701)
Interests earned on deposits, loans, and investments	(1,965)	(193)	—	5,630	3,472
Changes in operating assets and liabilities:					
Decrease in other assets	—	16	—	—	16
Increase (decrease) in accounts payable and accrued liabilities	(790)	(91)	507	38	(336)
Increase in deferred revenue	—	14	—	—	14
Increase (decrease) in compensated absences	(50)	102	—	—	52
Increase in disability and drivers benefits payable	30	126	—	—	156
Total adjustments	(2,883)	(68)	(1,919)	(457)	(5,327)
Net cash provided by (used in) operating activities	\$ (2,972)	925	15	(849)	(2,881)

## FIDUCIARY FUNDS

Fiduciary funds are used to account for assets held by the Commonwealth in a trustee capacity, or as an agent for individuals, private organizations, and other governmental units. The following are the Commonwealth's fiduciary funds:

### *Pension Trust Funds*

The pension trust funds are used to account for the assets, liabilities, and net assets available for pension benefits held in trust for the public employees of the Commonwealth.

**Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS):** ERS is the administrator of a defined-benefit pension plan which covers all regular employees of the Commonwealth and its instrumentalities and of certain municipalities and component units not covered by their own retirement systems. On September 24, 1999, an amendment to the Law that created ERS was enacted with the purpose of establishing a new defined contribution pension plan (System 2000) for persons joining the government on or after January 1, 2000.

**Puerto Rico Judiciary Retirement System (JRS):** JRS is administered by the ERS and covers all individuals holding a position as Justice of the Supreme Court, Judge of the former Superior Court, Judge of the District Court, or the Municipal Judges of the Commonwealth. The system provides retirement as well as death and disability benefits.

**Puerto Rico System of Annuities and Pensions for Teachers (TRS):** TRS provides retirement benefits to all teachers of the Department of Education of the Commonwealth, all pensioned teachers, all teachers transferred to an administrative position in the Department of Education, teachers who work in the Teachers' Association of Puerto Rico, and those who practice in private institutions accredited by the Department of Education. TRS provides retirement, death, and disability benefits.

### *Agency Fund*

Agency fund is used to account for assets held by the government as an agent for individuals, private organizations, and other governments. These funds are custodial in nature (assets equal liabilities) and do not involve measurement of the results of operations.

**Special Deposits:** This fund acts in a fiduciary capacity in order to account for moneys received with specified purposes for which the law does not address any other fund. It mainly includes deposits under the custody of the courts of justice for alimony payments.

# COMMONWEALTH OF PUERTO RICO

## Combining Statement of Fiduciary Net Assets – Pension Trust Funds

June 30, 2003

(In thousands)

Assets	Pension trust funds			Totals
	Employees' Retirement System (ERS)	Teachers' Retirement System (TRS)	Judiciary Retirement System (JRS)	
Cash and cash equivalents:				
Unrestricted	\$ 35,038	82,723	2,555	120,316
Restricted	—	2,236	—	2,236
Cash and cash equivalents in governmental banks:				
Unrestricted	28,112	4,199	990	33,301
Restricted	653	—	—	653
Investments:				
Debt and equity securities	1,197,086	1,831,092	59,831	3,088,009
Investment in PRTA Holdings, at appraised value	362,670	—	—	362,670
Other	—	34,735	—	34,735
Receivables, net:				
Accounts	44,976	—	—	44,976
Loans and advances	281,796	349,444	389	631,629
Accrued interests and dividends	4,052	9,702	350	14,104
Other	17,567	1,845	79	19,491
Other assets	17,395	25,562	—	42,957
Total assets	1,989,345	2,341,538	64,194	4,395,077
<b>Liabilities</b>				
Accounts payable and accrued liabilities	5,431	175,933	521	181,885
Securities lending transactions	36,512	—	1,892	38,404
Bonds payable	—	22,943	—	22,943
Total liabilities	41,943	198,876	2,413	243,232
<b>Net Assets</b>				
Net assets held in trust for pension and other benefits	\$ 1,947,402	2,142,662	61,781	4,151,845

# COMMONWEALTH OF PUERTO RICO

## Combining Statement of Changes in Fiduciary Net Assets – Pension Trust Funds

Year ended June 30, 2003

(In thousands)

	Pension trust funds			
	Employees' Retirement System (ERS)	Teachers' Retirement System (TRS)	Judiciary Retirement System (JRS)	Totals
Additions:				
Contributions:				
Sponsor	\$ 312,473	112,774	5,536	430,783
Participants	276,347	104,403	2,479	383,229
Special	17,931	27,490	—	45,421
Total contributions	606,751	244,667	8,015	859,433
Additions:				
Interests	43,309	82,210	1,804	127,323
Dividends	42,561	16,513	168	59,242
Net increase (decrease) in fair value of investments, including realized losses on sale and maturities of investments	(36,440)	(42,227)	2,414	(76,253)
Investment expenses	(3,425)	(5,508)	(255)	(9,188)
Net interest and investment income	46,005	50,988	4,131	101,124
Other income	11,127	1,010	—	12,137
Total additions	663,883	296,665	12,146	972,694
Deductions:				
Pension and other benefits	644,801	298,529	9,330	952,660
Refunds of contribution	22,589	3,021	—	25,610
General and administrative	28,768	19,544	1,473	49,785
Total deductions	696,158	321,094	10,803	1,028,055
Net change in net assets held in trust for pension and other benefits	(32,275)	(24,429)	1,343	(55,361)
Net assets held in trust for pension and other benefits:				
Beginning of year	1,979,677	2,167,091	60,438	4,207,206
End of year	\$ 1,947,402	2,142,662	61,781	4,151,845

# COMMONWEALTH OF PUERTO RICO

## Combining Statement of Changes in Assets and Liabilities – Agency Fund

Year ended June 30, 2003  
(In thousands)

	<b>Balance at June 30, 2002</b>	<b>Additions</b>	<b>Deletions</b>	<b>Balance at June 30, 2003</b>
<b>Assets</b>				
Cash and cash equivalents	\$ 205,883	300,317	—	506,200
Cash and cash equivalents in governmental banks	396,818	2,977,919	3,286,411	88,326
Investments	11,780	1,315	—	13,095
Accounts receivable, net	14,904	30,566	26,487	18,983
Other assets	533	—	51	482
Total assets	<u>\$ 629,918</u>	<u>3,310,117</u>	<u>3,312,949</u>	<u>627,086</u>
<b>Liabilities</b>				
Accounts payable and accrued liabilities	<u>\$ 629,918</u>	<u>3,310,117</u>	<u>3,312,949</u>	<u>627,086</u>
Total liabilities	<u>\$ 629,918</u>	<u>3,310,117</u>	<u>3,312,949</u>	<u>627,086</u>



## **NONMAJOR COMPONENT UNITS**

These entities are presented because the nature and significance of their relationship with the primary government are such that their exclusion would cause the basic financial statements to be misleading. These are discretely presented in a separate column in the basic financial statements due to the nature of the services they provide. The accounting principles followed by each of the component units included herein may vary depending on the type of industries these are involved (that is, banking, construction, public utilities, and so forth). The detailed information for each of these entities may be obtained directly from the administrative offices of the corresponding entities, as described in note 1, of the basic financial statements included in the financial section of this report.

# COMMONWEALTH OF PUERTO RICO

## Nonmajor Discretely Presented Component Units Statement of Net Assets

June 30, 2003  
(In thousands)

	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Municipal Finance Agency	Puerto Rico Ports Authority	Puerto Rico Industrial Development Company	Automobile Accident Compensation Administration	Puerto Rico Land Administration	National Parks Company of Puerto Rico
Assets:								
Current assets:								
Cash and cash equivalents	\$ 1,790	2,203	—	593	39,342	6,363	812	118
Cash and cash equivalents in governmental banks	—	190	2,062	—	—	—	14,971	(1,580)
Investments, including collateral from securities lending transactions	1,225,958	467,464	331,488	—	—	247,370	73,366	14,304
Receivables, net:								
Intergovernmental	—	—	—	—	—	—	—	13
Accounts	57,528	—	—	60,400	13,955	7,273	2,489	2,611
Loans and advances	—	41,058	—	—	—	—	—	—
Accrued interest	9,765	2,298	—	—	3,219	1,803	863	—
Other governmental entities	—	—	3,432	—	—	—	—	23
Other	19,461	—	—	—	—	1,299	5,868	—
Due from:								
Primary government	—	—	—	—	—	—	—	—
Component units	—	433	—	—	—	—	—	—
Inventories	7,433	—	—	733	—	—	—	—
Prepays	—	—	1	7,454	—	—	—	656
Total current assets	1,321,935	513,646	336,983	69,180	56,516	264,108	98,369	16,145
Noncurrent assets:								
Restricted assets:								
Cash and cash equivalents	—	—	—	47,144	51,141	—	—	(222)
Cash and cash equivalents in governmental banks	—	—	104	21,875	—	—	—	54,023
Investments and other restricted assets	—	—	1,569,496	—	37,007	—	—	17,551
Investments	—	218,251	—	—	3,000	—	—	—
Receivables:								
Loans, interest, and other	—	84,948	41,097	—	4,308	—	—	—
Due from:								
Component units	—	9,178	—	15,128	—	—	—	—
Property held for sale and future development	55,599	—	—	—	—	—	150,844	—
Capital assets, not being depreciated	13,010	—	—	330,264	313,586	901	7,621	25,087
Capital assets, depreciable, net	102,156	11,489	—	294,105	385,635	6,399	6,663	195,172
Deferred expenses and other assets	—	5,431	24,396	3,367	7,765	35	229	—
Total noncurrent assets	170,765	329,297	1,635,093	731,883	802,442	7,335	165,357	291,611
Total assets	\$ 1,492,700	\$ 842,943	\$ 1,972,076	\$ 801,063	\$ 858,958	\$ 271,443	\$ 263,726	\$ 307,756

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2003  
(In thousands)

	Puerto Rico Medical Services Administration	Puerto Rico Exports Development Corporation	Tourism Company of Puerto Rico	Puerto Rico and Caribbean Cardiovascular Center Corporation	Agricultural Services and Development Administration	Land Authority of Puerto Rico	Puerto Rico Metropolitan Bus Authority	Puerto Rico Telephone Authority
Assets:								
Current assets:								
Cash and cash equivalents	\$ 965	826	68,156	3,359	4	9,700	3,122	—
Cash and cash equivalents in governmental banks	—	354	257	—	—	—	—	401
Investments, including collateral from securities lending transactions	—	18,736	10,264	—	—	1,371	—	—
Receivables, net:								
Intergovernmental	—	—	—	—	—	—	1,973	—
Accounts	9,796	802	7,379	13,166	9,498	7,307	—	—
Loans and advances	—	—	507	—	—	581	—	—
Accrued interest	—	65	—	—	—	—	—	—
Other governmental entities	55,380	—	—	—	—	—	—	—
Other	—	—	—	1,057	98	28	923	—
Due from:								
Primary government	—	—	—	—	13,126	—	1,164	—
Component units	—	—	100,821	—	—	17,367	—	—
Inventories	3,551	—	—	1,704	10,356	108	6,402	—
Prepays	—	117	—	434	499	—	—	—
Total current assets	69,692	20,900	187,384	19,720	33,581	36,462	13,584	401
Noncurrent assets:								
Restricted assets:								
Cash and cash equivalents	\$ 5	—	—	5,347	3,944	—	—	—
Cash and cash equivalents in governmental banks	—	—	—	—	1,385	17,979	1,512	8,556
Investments and other restricted assets	—	9,611	10,000	—	—	—	—	94,980
Investments	—	—	—	—	—	—	—	—
Receivables:								
Loans, interest, and other	—	556	6,863	—	—	844	—	189
Due from:								
Component units	—	—	—	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—	—	—
Capital assets, not being depreciated	7,322	57,137	7,242	347	5,111	61,963	2,569	—
Capital assets, depreciable, net	22,685	35,940	16,125	43,299	26,994	10,605	59,782	—
Deferred expenses and other assets	—	—	8,060	—	540	—	—	—
Total noncurrent assets	30,012	103,244	48,290	48,993	37,974	91,391	63,863	103,725
Total assets	\$ 99,704	124,144	235,674	68,713	71,555	127,853	77,447	104,126

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2003  
(In thousands)

	Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental, Control Facilities Financing Authority	Puerto Rico Solid Waste Authority	Public Corporation for the Deposit Insurance of Puerto Rico	Right to Employment Administration	Puerto Rico Public Broadcasting Corporation
Assets:					
Current assets:					
Cash and cash equivalents	—	6,015	—	2,134	1,798
Cash and cash equivalents in governmental banks	37,088	—	579	11,669	—
Investments, including collateral from securities lending transactions	—	—	92,935	—	—
Receivables, net:					
Intergovernmental	—	143	—	945	—
Accounts	—	2,722	—	174	359
Loans and advances	—	—	—	—	—
Accrued interest	14	—	656	6	—
Other governmental entities	—	—	—	1,688	548
Other	—	—	235	—	29
Due from:					
Primary government	—	—	—	—	—
Component units	—	—	—	—	—
Inventories	—	—	—	—	—
Prepays	—	286	—	—	398
Total current assets	37,102	9,166	94,405	16,620	3,132
Noncurrent assets:					
Restricted assets:					
Cash and cash equivalents	—	1,345	—	—	10,857
Cash and cash equivalents in governmental banks	—	16,249	—	—	—
Investments and other restricted assets	—	533	—	—	—
Investments	—	950	—	—	—
Receivables:					
Loans, interest, and other	—	—	—	—	—
Due from:					
Component units	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—
Capital assets, not being depreciated	171,932	70,099	—	—	560
Capital assets, depreciable, net	—	56,489	313	473	12,946
Deferred expenses and other assets	4	—	—	—	1,081
Total noncurrent assets	171,936	145,665	313	473	25,444
Total assets	209,038	154,831	94,718	17,093	28,576

# COMMONWEALTH OF PUERTO RICO

## Nonmajor Discretely Presented Component Units Statement of Net Assets

June 30, 2003  
(In thousands)

	Fine Arts Center Corporation	Puerto Rico Maritime Transportation Authority	Puerto Rico Council on Higher Education	Farm Insurance Corporation of Puerto Rico	Employment and Training Enterprise Corporation	Caribbean Basin Projects Financing Authority	Puerto Rico Conservatory of Music Corporation
Assets:							
Current assets:							
Cash and cash equivalents	\$ 2,581	643	—	922	—	—	179
Cash and cash equivalents in governmental banks	—	—	9,664	—	275	5,175	—
Investments, including collateral from securities lending transactions	—	—	67	—	—	—	—
Receivables, net:							
Intergovernmental	—	—	—	—	—	—	—
Accounts	136	—	496	144	2,528	—	6,297
Loans and advances	—	—	—	—	—	—	—
Accrued interest	—	—	—	—	—	2	—
Other governmental entities	100	—	—	—	—	—	183
Other	—	—	—	—	—	—	8
Due from:							
Primary government	—	2,646	—	—	—	—	—
Component units	—	—	—	7,470	—	—	—
Inventories	—	960	—	—	1,162	—	—
Prepays	183	155	—	1,371	—	—	68
Total current assets	3,000	4,404	10,227	9,907	3,965	5,177	6,735
Noncurrent assets:							
Restricted assets:							
Cash and cash equivalents	1,098	—	—	2,125	—	—	12
Cash and cash equivalents in governmental banks	—	—	—	—	3,788	—	587
Investments and other restricted assets	—	—	—	—	—	—	—
Investments	—	—	—	—	—	—	—
Receivables:							
Loans, interest, and other	—	—	—	—	—	—	—
Due from:							
Component units	—	—	—	—	—	—	—
Property held for sale and future development	—	—	—	—	—	—	—
Capital assets, not being depreciated	2,929	8,102	—	—	—	—	13,213
Capital assets, depreciable, net	15,065	40,671	698	139	538	—	1,773
Deferred expenses and other assets	—	—	—	—	—	—	—
Total noncurrent assets	19,092	48,773	698	2,264	4,326	—	15,585
Total assets	\$ 22,092	53,177	10,925	12,171	8,291	5,177	22,320

# COMMONWEALTH OF PUERTO RICO

## Nonmajor Discretely Presented Component Units Statement of Net Assets

June 30, 2003  
(In thousands)

Assets:	Musical Arts Corporation	Puerto Rico School of Plastic Arts	Corporation for the Development of the Arts, Sciences, and Film Industry	Governing Board of the 911 Service	Special Communities Perpetual Trust	Puerto Rico Convention Center District Authority	Total
<b>Current assets:</b>							
Cash and cash equivalents	2,945	11	—	—	—	8,920	163,501
Cash and cash equivalents in governmental banks	—	887	633	22,700	781	—	106,106
Investments, including collateral from securities lending transactions	—	—	—	—	—	—	2,483,323
Receivables, net:							
Intergovernmental	—	—	—	—	—	—	3,074
Accounts	66	—	—	2,097	—	3,717	210,940
Loans and advances	—	—	—	255	—	—	42,401
Accrued interest	—	—	—	47	—	—	18,738
Other governmental entities	268	—	—	—	188	—	61,810
Other	10	—	—	—	—	—	29,016
Due from:							
Primary government	—	—	—	—	—	—	16,936
Component units	—	—	—	—	—	—	126,091
Inventories	—	—	—	—	—	—	32,409
Prepays	—	—	—	21	—	2,475	14,122
Total current assets	3,289	898	633	25,120	969	15,112	3,308,467
<b>Noncurrent assets:</b>							
Restricted assets:							
Cash and cash equivalents	32	—	—	—	—	—	122,828
Cash and cash equivalents in governmental banks	—	—	6,816	—	—	—	132,874
Investments and other restricted assets	—	300	—	—	—	—	1,729,478
Investments	—	—	—	—	—	—	232,201
Receivables:							
Loans, interest, and other	—	—	—	893	—	—	139,698
Due from:							
Component units	—	—	—	—	—	—	24,306
Property held for sale and future development	—	—	—	—	—	—	206,443
Capital assets not being depreciated	153	—	—	—	—	173,882	1,293,030
Capital assets, depreciable, net	181	1,165	34	104	—	113	1,347,751
Deferred expenses and other assets	—	—	—	—	—	—	50,908
Total noncurrent assets	366	1,465	6,850	997	—	173,995	5,279,517
Total assets	3,655	2,363	7,483	26,117	969	189,107	8,587,984

**COMMONWEALTH OF PUERTO RICO**  
**Nonmajor Discretely Presented Component Units**  
**Statement of Net Assets**

June 30, 2003  
(In thousands)

	State Insurance Fund Corporation	Economic Development Bank for Puerto Rico	Puerto Rico Municipal Finance Agency	Puerto Rico Ports Authority	Puerto Rico Industrial Development Company	Automobile Accident Compensation Administration	Puerto Rico Land Administration	National Parks Company of Puerto Rico
<b>Liabilities and Net Assets</b>								
<b>Liabilities:</b>								
Current liabilities:								
Accounts payable and accrued liabilities	\$ 127,118	3,391	4,984	84,593	48,516	10,408	5,185	11,212
Deposits and escrow liabilities	—	468,704	248,052	1,244	5,520	—	1,652	—
Due to:								
Primary government	—	—	—	—	—	—	—	—
Component units	—	279	—	238,493	78,666	—	—	—
Other governmental entities	—	—	—	—	—	—	—	1,204
Securities lending transactions and reverse repurchase agreements	77,938	55,000	—	—	—	49,843	—	—
Interest payable	—	1,151	35,200	2,847	4,673	—	—	—
Deferred revenue	46,389	—	230	663	—	35,884	—	—
Notes payable, current portion	1,135	5,317	—	25,162	1,215	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	—	—	—	—
Bonds payable, current portion	—	—	85,636	8,380	9,585	—	—	—
Accrued compensated absences	31,232	—	—	7,176	—	3,070	842	273
Reserves for automobile accident benefit payments	865,352	—	—	—	—	113,562	—	—
Current portion of other long-term liabilities	664	3,823	—	9,362	730	—	—	183
Total current liabilities	1,149,828	537,665	374,102	377,920	148,905	212,767	7,679	12,872
Noncurrent liabilities:								
Due to:								
Primary government	—	—	—	—	—	—	—	—
Component units	—	12,816	—	12,000	56	—	—	—
Securities lending transactions and reverse repurchase agreements	—	27,300	—	—	—	—	—	—
Deferred revenue	—	—	2,800	2,525	—	—	—	—
Notes payable	56,638	155,234	—	21,900	57,757	—	—	—
Commonwealth appropriation bonds	—	—	—	—	—	—	—	—
Bonds payable	—	—	1,338,474	73,877	167,660	—	—	—
Accrued compensated absences	—	1,667	—	—	—	—	—	3,854
Other long-term liabilities	66,697	499	88,462	369	139	—	38,530	977
Total noncurrent liabilities	123,335	197,516	1,429,736	110,671	225,612	—	38,530	4,831
Total liabilities	1,273,163	735,181	1,803,838	488,591	374,517	212,767	46,209	17,703
<b>Net assets:</b>								
Invested in capital assets, net of related debt	78,485	(1,606)	—	343,571	380,061	—	6,770	220,259
Capital projects	—	—	—	23,507	—	—	—	—
Debt service	—	—	—	30,573	—	—	—	—
Student loans and other educational purposes	—	—	—	—	—	—	—	—
Other specified purposes	141,052	8,278	84,292	5,575	102,051	—	—	—
Unrestricted	—	101,090	83,946	(90,754)	2,329	58,676	210,747	69,794
Total net assets	219,537	107,762	168,238	312,472	484,441	58,676	217,517	290,053
Total liabilities and net assets	\$ 1,492,700	\$ 842,943	\$ 1,972,076	\$ 801,063	\$ 858,958	\$ 271,443	\$ 263,726	\$ 307,756

COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net Assets

June 30, 2003  
(In thousands)

	Puerto Rico Medical Services Administration	Puerto Rico Exports Development Corporation	Tourism Company of Puerto Rico	Puerto Rico and Caribbean Cardiovascular Center Corporation	Agricultural Services and Development Administration	Land Authority of Puerto Rico	Puerto Rico Metropolitan Bus Authority	Puerto Rico Telephone Authority
<b>Liabilities and Net Assets</b>								
<b>Liabilities:</b>								
Current liabilities:								
Accounts payable and accrued liabilities	\$ 62,158	2,803	38,966	24,465	36,329	68,114	26,142	39,822
Deposits and escrow liabilities	—	—	—	—	—	8,246	—	—
Due to:								
Primary government	—	—	—	—	—	—	—	—
Component units	23,114	433	105,392	—	24,837	28,652	5,428	—
Other governmental entities	7,807	—	—	—	8,015	—	—	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—	—	—	—
Interest payable	—	107	—	14,185	2,631	5,861	72	—
Deferred revenue	—	—	—	—	5,183	346	186	—
Notes payable, current portion	—	—	—	—	—	1,134	—	—
Commonwealth appropriation bonds, current portion	—	—	1,302	—	—	—	—	—
Bonds payable, current portion	—	—	1,286	1,738	—	—	—	—
Accrued compensated absences	5,922	—	—	—	9,041	1,314	3,939	—
Reserves for automobile accident benefit payments	—	—	—	—	—	—	—	—
Current portion of other long-term liabilities	1,813	—	1,492	7,083	—	8,510	—	—
Total current liabilities	100,814	3,343	148,438	47,471	86,036	122,177	35,767	39,822
<b>Noncurrent liabilities:</b>								
Due to:								
Primary government	—	—	—	25,597	—	—	—	—
Component units	—	9,178	—	—	20,498	43,943	—	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—	—	—	—
Deferred revenue	—	—	—	—	—	—	—	—
Notes payable	—	—	—	—	—	—	—	—
Commonwealth appropriation bonds	—	—	126,006	—	—	109,927	—	—
Bonds payable	—	—	—	—	—	—	—	—
Accrued compensated absences	—	693	4,061	—	—	—	—	—
Other long-term liabilities	10,249	3,333	500	27,666	582	—	—	37,817
Total noncurrent liabilities	10,249	13,204	130,567	53,263	21,080	153,870	—	37,817
Total liabilities	111,063	16,547	279,005	100,734	107,116	276,047	35,767	77,639
<b>Net assets:</b>								
Invested in capital assets, net of related debt	24,909	83,466	23,185	42,160	—	72,568	62,352	—
Capital projects	—	—	—	3,847	—	—	41	—
Debt service	—	—	—	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	—	—	—	—
Other specified purposes	5	—	—	—	(8,038)	—	—	26,223
Unrestricted	(36,273)	24,131	(66,516)	(78,028)	(27,523)	(220,762)	(20,713)	264
Total net assets	(11,359)	107,597	(43,331)	(32,021)	(35,561)	(148,194)	41,680	26,487
Total liabilities and net assets	\$ 99,704	124,144	235,674	68,713	71,555	127,853	77,447	104,126



# COMMONWEALTH OF PUERTO RICO

## Nonmajor Discretely Presented Component Units Statement of Net Assets

June 30, 2003  
(In thousands)

Liabilities and Net Assets	Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental, Control Facilities Financing Authority	Puerto Rico Solid Waste Authority	Public Corporation for the Deposit Insurance of Puerto Rico	Right to Employment Administration	Puerto Rico Public Broadcasting Corporation
<b>Liabilities:</b>					
Current liabilities:					
Accounts payable and accrued liabilities	2,421	12,871	33,763	3,157	3,295
Deposits and escrow liabilities	—	—	—	—	—
Due to:					
Primary government	—	—	—	—	—
Component units	128,302	7,608	—	—	—
Other governmental entities	—	—	—	1,640	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—
Interest payable	2,610	—	—	—	—
Deferred revenue	—	—	—	—	—
Notes payable, current portion	—	—	—	9,455	10,857
Commonwealth appropriation bonds, current portion	—	228	—	—	—
Bonds payable, current portion	—	—	—	—	—
Accrued compensated absences	—	245	869	1,239	750
Reserves for automobile accident benefit payments	—	—	—	—	—
Current portion of other long-term liabilities	82	57	—	—	54
Total current liabilities	133,415	21,009	34,632	15,491	14,956
Noncurrent liabilities:					
Due to:					
Primary government	—	—	—	—	—
Component units	—	—	—	—	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—
Deferred revenue	—	—	—	—	—
Notes payable	—	—	—	—	—
Commonwealth appropriation bonds	—	21,764	—	—	—
Bonds payable	—	—	—	—	—
Accrued compensated absences	—	653	—	1,401	1,183
Other long-term liabilities	—	115	—	—	—
Total noncurrent liabilities	—	22,532	—	1,401	1,183
Total liabilities	133,415	43,541	34,632	16,892	16,139
<b>Net assets:</b>					
Invested in capital assets, net of related debt	31,219	96,873	314	473	13,452
Capital projects	—	—	—	—	—
Debt service	—	—	—	—	—
Student loans and other educational purposes	—	—	—	—	—
Other specified purposes	—	2,062	50,685	—	—
Unrestricted	44,404	12,355	9,087	(272)	(1,015)
Total net assets	75,623	111,290	60,086	201	12,437
<b>Total liabilities and net assets</b>	<b>209,038</b>	<b>154,831</b>	<b>94,718</b>	<b>17,093</b>	<b>28,576</b>

## COMMONWEALTH OF PUERTO RICO

Nonmajor Discretely Presented Component Units  
Statement of Net AssetsJune 30, 2003  
(In thousands)

Liabilities:	Fine Arts Center Corporation	Puerto Rico Maritime Transportation Authority	Puerto Rico Council on Higher Education	Farm Insurance Corporation of Puerto Rico	Employment and Training Enterprise Corporation	Caribbean Basin Projects Financing Authority	Puerto Rico Conservatory of Music Corporation
Liabilities and Net Assets							
Current liabilities:							
Accounts payable and accrued liabilities	\$ 285	4,416	1,215	4,354	11,725	8	503
Deposits and escrow liabilities	485	41	—	—	—	—	—
Due to:							
Primary government	—	—	—	—	—	—	—
Component units	—	—	—	—	721	—	—
Other governmental entities	3	—	—	175	—	—	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—	—	—
Interest payable	—	—	—	—	149	—	—
Deferred revenue	1,586	—	—	165	788	—	130
Notes payable, current portion	—	—	—	—	—	—	—
Commonwealth appropriation bonds, current portion	—	—	—	—	—	—	—
Bonds payable, current portion	—	—	—	—	—	—	—
Accrued compensated absences	109	695	—	327	180	—	141
Reserves for automobile accident benefit payments	—	—	—	—	—	—	—
Current portion of other long-term liabilities	11	601	—	—	—	—	—
Total current liabilities	2,479	5,753	1,215	5,021	13,563	8	774
Noncurrent liabilities:							
Due to:							
Primary government	—	—	—	—	—	—	—
Component units	—	15,128	—	—	1,414	—	—
Securities lending transactions and reverse repurchase agreements	—	—	—	—	—	—	—
Deferred revenue	—	—	—	—	—	—	—
Notes payable	—	—	—	—	—	—	—
Commonwealth appropriation bonds	—	—	—	—	—	—	—
Bonds payable	—	—	—	—	—	—	—
Accrued compensated absences	207	—	300	—	—	—	712
Other long-term liabilities	9	—	—	—	—	—	—
Total noncurrent liabilities	216	15,128	300	—	1,414	—	712
Total liabilities	2,695	20,881	1,515	5,021	14,977	8	1,486
Net assets:							
Invested in capital assets, net of related debt	17,974	48,773	698	139	538	—	14,856
Capital projects	—	—	—	—	—	—	—
Debt service	—	—	—	—	—	—	—
Student loans and other educational purposes	—	—	7,864	—	—	—	—
Other specified purposes	1,098	—	—	2,125	504	—	591
Unrestricted	325	(16,477)	848	4,886	(7,728)	5,169	5,387
Total net assets	19,397	32,296	9,410	7,150	(6,686)	5,169	20,834
Total liabilities and net assets	22,092	53,177	10,925	12,171	8,291	5,177	22,320
\$							

**Nonmajor Discretely Presented Component Units  
Statement of Net Assets**

June 30, 2003  
(In thousands)

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(Continued)

**COMMONWEALTH OF PUERTO RICO**  
Nonmajor Discretely Presented Component Units  
Statement of Activities  
Year ended June 30, 2003  
(In thousands)

	General revenue and transfers										Net assets, end of year	
	Program revenue					Grants and contributions not restricted to specific programs		Interest and investment earnings		Change in net assets		
	Expenses	Charges for services	Operating grants and contributions	Capital grants and contributions	Net revenue (expenses) and changes in net assets	Payments from primary government	Taxes	Gain (loss) in sale of assets	Miscellaneous			
State Insurance Fund Corporation	\$ 450,024	575,944	—	—	125,920	—	—	90,953	—	216,873	2,664	219,537
Economic Development Bank for Puerto Rico	25,261	26,598	—	—	1,337	—	—	—	—	1,337	106,425	107,762
Puerto Rico Ports Authority	138,841	118,858	—	12,534	(7,449)	—	—	1,107	—	9,227	303,245	312,472
Puerto Rico Municipal Finance Agency	70,423	—	—	—	(70,423)	—	—	149,946	—	79,523	88,715	168,238
Puerto Rico Industrial Development Company	87,902	51,418	—	509	(35,975)	36,259	—	4,270	14,078	18,632	465,809	484,441
Puerto Rico Telephone Authority	71,563	3	—	—	(71,560)	—	—	(876)	—	(72,436)	98,923	26,487
Automobile Accident Compensation Administration	96,389	75,169	—	—	(21,220)	—	—	8,130	—	(13,090)	71,766	58,676
Puerto Rico Land Administration	9,039	16,972	—	—	7,933	—	—	1,510	—	3,542	213,975	217,517
National Parks Company of Puerto Rico	40,938	10,157	—	—	(30,781)	53,700	457	1,037	—	27,604	262,449	290,053
Puerto Rico Medical Services Administration	121,696	88,071	—	—	(33,625)	21,373	—	143	—	3,191	750	(11,359)
Puerto Rico Exports Development Corporation	12,721	14,396	—	—	1,675	—	—	238	—	2,006	105,591	107,597
Tourism Company of Puerto Rico	283,085	233,751	—	—	(49,334)	13,957	—	34,278	—	648	(43,331)	107,331
Puerto Rico and Caribbean Cardiovascular Center Corporation	61,853	50,286	—	—	(11,567)	4,100	—	145	—	(7,322)	(24,699)	(32,021)
Agricultural Services and Development Administration	188,271	70,739	—	—	(117,532)	91,723	—	—	—	(4,620)	(5,132)	(35,561)
Land Authority of Puerto Rico	41,895	17,438	—	—	(24,457)	5,751	—	9,621	(3,571)	(11,555)	(136,639)	(148,194)
Puerto Rico Metropolitan Bus Authority	76,020	21,187	—	18,313	(36,520)	22,269	—	75	—	(14,176)	55,856	41,680
Puerto Rico Industrial, Tourist, Educational, Medical, and Environmental Control Facilities Financing Authority	537	938	—	—	401	22,000	—	287	—	22,688	52,935	75,623
Puerto Rico Solid Waste Authority	13,517	1,118	65	—	(12,394)	20,723	—	427	—	6,592	104,698	111,290
Public Corporation for the Supervision and Deposit Insurance of Puerto Rico	5,185	7,783	4,161	—	6,759	—	—	2,219	—	8,978	51,108	60,086
Right to Employment Administration	53,275	—	10,421	—	(42,854)	42,463	—	121	—	(159)	360	201
Puerto Rico Public Broadcasting Corporation	30,533	1,502	—	—	(29,031)	25,669	2,396	223	—	381	12,799	12,437
Fine Arts Center Corporation	5,010	2,295	—	—	(2,715)	3,137	—	142	—	564	18,833	19,397
Puerto Rico Maritime Transportation Authority	30,664	4,105	—	349	(26,210)	15,500	—	4	—	(10,706)	43,002	32,296
Puerto Rico Council on Higher Education	30,646	104	—	1,303	(29,239)	26,960	—	146	—	(2,111)	11,521	9,410
Farm Insurance Corporation of Puerto Rico	5,038	4,701	—	—	(337)	—	—	55	—	264	6,886	7,150
Employment and Training Enterprise Corporation	6,990	7,033	131	—	174	906	—	287	—	1,367	(8,053)	(6,686)
Caribbean Basin Projects Financing Authority	5	—	—	—	(5)	—	—	40	—	35	5,134	5,169
Puerto Rico Conservatory of Music Corporation	6,072	1,523	605	—	(3,944)	3,797	—	8	—	(34)	20,868	20,834
Musical Arts Corporation and Subsidiaries	8,684	502	266	—	(7,916)	6,578	553	516	—	(269)	514	245
Puerto Rico School of Plastic Arts	3,797	435	836	—	(2,526)	3,219	—	—	—	693	944	1,637
Corporation for the Development of the Arts, Sciences, and Film Industry of Puerto Rico	1,187	180	—	—	(1,007)	2,341	—	3,225	—	4,559	2,585	7,144
Governing Board of the 911 Service	12,827	18,651	—	—	5,824	—	—	—	—	6,549	13,280	19,829
Special Communities Perpetual Trust	5,878	—	480	—	(5,398)	—	—	—	—	(5,356)	—	(5,356)
Puerto Rico Convention Center District Authority	4,155	—	—	—	(4,155)	60,000	—	2,099	—	57,998	4,324	62,322
Total nonmajor component units	\$ 1,999,921	\$ 1,421,857	\$ 16,965	\$ 33,008	\$ (528,091)	\$ 482,425	\$ 3,406	\$ 49,739	\$ 263,676	\$ 10,507	\$ 1,907,457	\$ 2,197,022

## **STATISTICAL SECTION**

**COMMONWEALTH OF PUERTO RICO**

**General Governmental Expenditures by Function  
All Governmental Fund Types**

**For the last ten fiscal years  
(In thousands)**

Function:	2003	%	2002*	2001	2000	1999	1998	1997	1996	1995	1994
<b>General government</b>	\$ 1,774,156	12.3%	1,279,750	739,009	853,040	526,629	484,547	499,652	661,359	451,275	341,066
Public safety	1,424,846	9.9%	1,659,280	1,623,362	1,310,322	1,103,606	1,241,762	1,188,814	926,498	878,673	798,367
Health	1,908,717	13.2%	1,983,727	954,563	972,757	625,475	656,498	508,659	245,743	231,212	192,118
Public housing and welfare	2,953,189	20.4%	2,726,129	2,315,899	2,102,410	2,485,092	1,902,902	2,086,828	1,701,434	1,681,688	1,524,344
Education	3,297,248	22.8%	3,343,002	2,308,479	2,436,267	2,272,903	2,744,630	1,960,185	1,832,271	1,760,784	1,511,610
Economic development	428,621	3.0%	637,794	170,937	337,255	314,897	186,296	333,290	88,143	154,796	235,915
Intergovernmental	465,699	3.2%	466,169	222,721	373,016	318,664	55,739	496,844	306,226	207,389	184,261
Capital outlays	1,184,976	8.2%	507,634	1,020,344	833,597	642,016	1,515,230	1,395,463	1,255,430	848,801	549,352
Debt service:											
Principal	330,346	2.3%	2,062,059	466,467	416,369	351,722	620,866	359,851	367,198	660,133	317,561
Interest and other	685,461	4.7%	614,347	545,001	444,595	442,614	595,053	556,835	504,480	435,549	348,260
<b>Total expenditures</b>	<b>\$ 14,453,259</b>	<b>100.0%</b>	<b>15,279,891</b>	<b>10,366,782</b>	<b>10,079,628</b>	<b>9,083,618</b>	<b>10,003,523</b>	<b>9,386,421</b>	<b>7,888,782</b>	<b>7,310,300</b>	<b>6,002,854</b>
<b>All governmental fund types</b>											

\*In 2002 the Commonwealth adopted GASB Statement No. 34. This statement requires payments to component units to be included as expenditure by function. In prior years such payments were reported as operating transfers out to component units.

**COMMONWEALTH OF PUERTO RICO**

**General Governmental Revenue by Source  
All Governmental Fund Types**

**For the last ten fiscal years  
(In thousands)**

Source:	2003	%	2002*	2001	2000	1999	1998	1997	1996	1995	1994
<b>Taxes:</b>											
Income	\$ 4,874,795	40.0%	4,843,852	4,536,840	4,967,138	4,413,860	3,989,239	3,622,988	3,396,724	3,242,876	2,876,542
Property	122,666	1.0%	102,554	—	—	—	—	—	—	—	—
Excise	1,894,729	15.6%	1,713,098	1,788,992	1,736,539	1,714,444	1,884,348	1,827,305	1,713,537	1,664,529	1,589,770
Other	3,055	0.0%	1,963	92,024	87,523	78,926	73,426	64,910	57,662	56,536	53,521
Charges for services	780,905	6.4%	535,423	645,806	617,020	457,454	569,096	464,034	461,736	455,500	236,609
Intergovernmental	4,107,706	33.7%	3,634,358	3,807,049	2,971,528	3,435,765	3,009,169	3,077,042	2,545,615	2,492,443	2,328,427
Interest and investment earnings	85,565	0.7%	90,940	67,020	91,525	97,880	116,030	110,777	59,788	—	—
Other	314,002	2.6%	736,686	270,711	383,548	162,228	189,476	134,819	186,591	170,025	144,227
<b>Total revenue -</b>											
<b>All governmental fund types</b>	\$ 12,183,423	100.0%	11,658,874	11,208,442	10,854,821	10,360,557	9,830,784	9,301,875	8,421,653	8,081,929	7,229,096

\*The annual special tax of 1.03% of the assessed value of all real and personal property not exonerated from taxation, collected by the Municipal Revenue Collection Center on the Commonwealth's behalf, is presented as property tax in 2003 and 2002 but as intergovernmental revenue in prior years.

**COMMONWEALTH OF PUERTO RICO**

**Computation of the Legal Debt Margin**

**July 1, 2003**  
**(In thousands)**

<b>Statutory Margin</b>	
<b>Section 2, Article VI of the Constitution of Puerto Rico</b>	
<b>(Section 2, Article VI of the Constitution of Puerto Rico)</b>	
<b>Internal revenue for the year ended June 30, 2002</b>	<b>\$ 6,865,454</b>
<b>Internal revenue for the year ended June 30, 2003 (p)</b>	<b>7,505,866</b>
<b>Total internal revenue for the years ended June 30, 2002 and 2003</b>	<b>\$ 14,371,320</b>
<b>Internal revenue average for the two years</b>	<b>\$ 7,185,660</b>
<b>Legal debt limit – 15% of internal revenue average for the two years</b>	<b>\$ 1,077,849</b>
<b>Maximum debt service requirement – 8.345% on Commonwealth Bonds maturing on 2003 and PRASA debt service paid during fiscal year 2003</b>	<b>599,611</b>
<b>Additional legal debt service requirement margin</b>	<b>\$ 478,238</b>

**(p) Preliminary**

**Source: Government Development Bank for Puerto Rico.**



**COMMONWEALTH OF PUERTO RICO**

**Ratio of Annual Debt Service for General  
Bonded Debt to Total General Expenditures**

**For the last ten fiscal years  
(In thousands)**

<b>Fiscal year</b>	<b>Total debt service</b>	<b>General governmental expenditures</b>	<b>Ratio (%)</b>
2003	362,136	14,453,259	2.5%
2002	608,674	15,279,891	4.0
2001	538,436	10,366,782	5.2
2000	507,336	10,079,628	5.0
1999	468,970	9,083,618	5.2
1998	435,894	10,003,523	4.4
1997	430,153	9,386,421	4.6
1996	424,753	7,888,782	5.4
1995	389,278	7,310,300	5.3
1994	362,294	6,002,854	6.0

# COMMONWEALTH OF PUERTO RICO

## Demographic Statistics

For the last ten fiscal years

Fiscal year		Population*	Per capita income	Median age	School enrollment**	Unemployment rate (%)
2003	(p)	3,879	\$11,279	33.3	875,831	12.1
2002		3,863	10,969	32.9	792,284	12.0
2001		3,840	10,733 r	32.6	799,933 r	10.5
2000		3,800	10,204 r	32.2	799,322 r	11.0
1999		3,765	9,659 r	31.8	753,705	12.5
1998		3,732	9,108 r	31.4	753,428	13.6
1997		3,700	8,729 r	31.0	749,938	13.1
1996		3,670	8,076 r	30.7	770,537	13.8
1995		3,641	7,468 r	30.3	709,559	13.8
1994		3,614	7,120 r	29.9	714,705	16.0

\* Amounts expressed in thousands

\*\* The enrollment in private schools is an estimate

p Preliminary

r Revised

Source: Puerto Rico Planning Board, Puerto Rico Department of Education, and the General Council of Education

# COMMONWEALTH OF PUERTO RICO

## Construction and Bank Deposits

For the last ten fiscal years

Fiscal year	Commercial construction (1)		Residential construction (1)		(2) Bank deposits *
	Number of permits	Value *	Number of permits	Value *	
2003	288	\$ 167,697	7,155	\$ 1,016,007	\$45,895,052
2002	317	182,930	5,206	943,040	39,219,512
2001	368	170,388	4,990	932,128	37,788,557
2000	358	251,003	6,578	991,834	30,449,860
1999	286	106,186	6,498	694,714	28,423,313
1998	351	147,486	6,732	631,465	25,354,086
1997	354	149,121	6,159	635,343	23,191,572
1996	291	89,405	6,180	582,186	24,191,572
1995	346	126,021	6,678	674,797	22,876,069
1994	37	81,087	6,677	470,158	19,350,635

\* Amounts expressed in thousands

(1) Source: Puerto Rico Planning Board.

(2) Source: Commissioner of Financial Institutions

# COMMONWEALTH OF PUERTO RICO

## Miscellaneous Statistics

June 30, 2003

Statistic	Quantity
Population (millions)	3.9 (p)
Life expectancy	76.8
Area in square miles	3,426
Fire protection:	
Number of stations	93
Number of fire personnel and officers	1,894
Calls answered	12,340
Building inspections conducted	53,750
Police protection:	
Number of stations	228
Police personnel and officers	21,079
Total police vehicles	5,538
Water system:	
Customers	1,222,800
Water consumption ( millions of cubic meter )	399
Electric distribution system:	
Customers	1,401,301
Electricity consumption (millions of kilowatt)	19,887
Electricity production (millions of kilowatt)	23,717
Education:	
Enrollment in public schools:	
Kindergarden to sixth grade	326,606
Seventh to ninth grade	146,896
Tenth to twelfth grade	118,519
Enrollment in private schools:	
Kindergarden to sixth grade	172,479
Seventh to ninth grade	62,574
Tenth to twelfth grade	48,757
Enrollment in universities and colleges:	
Public	74,801
Private	125,041

(p)

Preliminary

Source: Various Commonwealth Public Agencies.

**COMMONWEALTH OF PUERTO RICO**

**General Fund Net Revenue**

For the last ten fiscal years  
(In thousands)

	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003*
<b>TOTAL</b>										
FROM INTERNAL REVENUE	4,665,331	5,080,139	5,247,616	5,600,748	5,902,506	6,550,043	6,943,613	6,962,134	7,454,399	7,841,742
TAX REVENUE	4,357,569	4,780,492	4,974,918	5,335,879	5,630,040	6,271,392	6,647,632	6,632,090	6,865,454	7,505,866
PROPERTY TAXES	4,111,119	4,531,788	4,729,320	5,095,218	5,358,805	5,982,504	6,344,398	6,204,639	6,428,083	6,910,345
INCOME TAXES, TOTAL	4,567	7,889	5,107	8,286	5,673	2,214	1,131	287	—	—
INDIVIDUALS	2,856,134	3,220,937	3,368,175	3,610,016	3,972,869	4,433,804	4,856,011	4,778,590	4,878,418	5,170,294
CORPORATIONS	1,409,824	1,578,269	1,709,116	1,825,337	2,026,612	2,244,376	2,352,066	2,259,090	2,449,982	2,767,678
PARTNERSHIPS	1,107,265	1,304,612	1,348,160	1,440,691	1,527,415	1,653,762	1,781,862	1,696,766	1,706,137	1,776,985
WITHHOLDING TO NONRESIDENTS	1,802	3,391	3,323	2,120	4,404	2,087	2,339	3,026	2,670	2,101
TOLLGATE TAX (REGULAR)	73,626	79,072	78,235	88,603	192,463	369,384	557,276	696,835	583,256	517,141
TOLLGATE TAX (PREPAYMENT)	130,829	110,945	78,554	83,640	65,285	49,249	57,203	23,664	44,213	35,576
INTEREST SUBJECT TO 17%	93,527	109,928	100,900	126,605	105,668	65,284	53,927	25,847	15,302	9,745
TAXES ON DIVIDENDS	5,293	6,070	6,662	7,582	11,406	10,666	11,674	14,782	14,310	11,278
INHERITANCE AND GIFT TAXES	33,968	28,650	43,225	35,438	39,616	38,996	39,664	58,580	62,548	49,790
EXCISE TAXES, TOTAL	934	1,535	1,547	4,028	1,380	1,811	3,109	7,475	1,962	2,825
ALCOHOLIC BEVERAGES, TOTAL	1,200,400	1,252,327	1,304,024	1,419,353	1,312,716	1,473,827	1,410,346	1,341,949	1,465,128	1,651,350
DISTILLED SPIRITS	220,882	222,187	237,915	229,043	238,118	243,464	236,374	237,512	249,705	299,582
BEER	45,864	50,586	54,934	51,855	48,034	47,519	49,425	46,963	51,734	58,389
OTHER BEVERAGES	168,555	162,630	172,425	167,321	178,465	181,348	170,065	177,448	179,737	223,309
GENERAL TAXES, TOTAL	6,463	8,971	10,556	9,867	11,619	14,597	16,884	13,101	18,234	17,884
CIGARETTES	979,518	1,030,140	1,066,109	1,190,310	1,074,598	1,230,363	1,173,972	1,104,437	1,215,423	1,351,768
PETROLEUM PRODUCTS	115,453	107,943	107,177	120,287	111,094	119,105	115,157	119,135	116,055	149,487
MOTOR VEHICLE	12,782	16,706	20,006	22,095	6,172	5,562	4,689	7,046	5,095	5,860
HORSE RACES	275,654	319,676	307,931	365,820	350,004	411,573	389,995	406,252	418,024	499,252
INSURANCE PREMIUMS	28,899	30,828	29,535	29,138	27,401	21,405	26,351	18,893	22,033	28,872
CEMENT	22,687	20,942	20,748	19,430	19,364	20,368	21,564	22,845	24,290	26,771
SLOT MACHINES	1,773	1,849	1,901	2,234	1,702	2,417	2,531	2,707	3,426	3,279
CRUDE OIL AND DERIVED PRODUCTS	—	—	—	—	12,230	26,330	30,869	—	36,953	90,018
5% GENERAL EXCISE TAX	152,911	139,594	157,742	158,739	51,636	70,056	24,786	1,901	38,619	12,925
HOTEL ROOMS	346,015	367,545	396,689	446,500	468,425	520,551	525,561	508,972	486,302	505,709
OTHERS	9,152	10,800	11,237	12,139	13,299	15,923	17,275	—	—	9,056
LICENSES	14,192	14,257	13,143	13,928	13,271	17,273	15,194	16,686	64,626	20,539
MOTOR VEHICLES	49,084	49,100	50,467	53,535	66,167	70,848	73,801	76,338	82,575	85,876
ENTERTAINMENT MACHINES	39,257	38,530	39,667	42,354	46,268	46,781	49,133	49,834	54,896	58,426
ALCOHOLIC BEVERAGES AND OTHERS	—	—	—	—	7,327	10,545	11,322	12,874	13,932	13,518
NON TAX REVENUE	9,827	10,570	10,800	11,181	12,572	14,832	14,123	15,182	14,805	13,518
TRADITIONAL LOTTERY	246,450	248,704	245,598	240,661	271,235	288,888	303,234	427,451	437,371	595,521
ELECTRONIC LOTTERY	62,348	63,317	60,856	52,829	57,986	59,206	63,779	57,482	61,358	67,621
TRANSFER FROM NONBUDGETED FUNDS	52,193	59,414	57,008	47,994	54,681	53,013	70,209	70,211	57,897	89,443
MISCELLANEOUS	—	—	—	—	—	—	—	89,093	80,000	123,600
FROM NONINTERNAL REVENUE	131,909	125,973	127,734	139,838	158,568	176,669	169,246	210,665	238,116	314,857
CUSTOM DUTIES	307,762	299,647	272,698	264,869	272,466	278,651	295,981	330,044	344,848	335,876
EXCISES ON OFF-SHORE SHIPMENTS	122,477	112,153	77,781	61,114	72,206	61,355	50,231	43,154	30,595	25,918
ADMINISTRATIVE MEASURES	185,285	187,494	194,917	203,755	200,260	217,296	245,750	286,890	314,253	309,598
	—	—	—	—	—	—	—	—	244,097	—

Note: The net revenue presented above includes the actual revenue and the operating transfers from other funds presented in the combined statement of revenue and expenditures - budget and actual - budget basis.

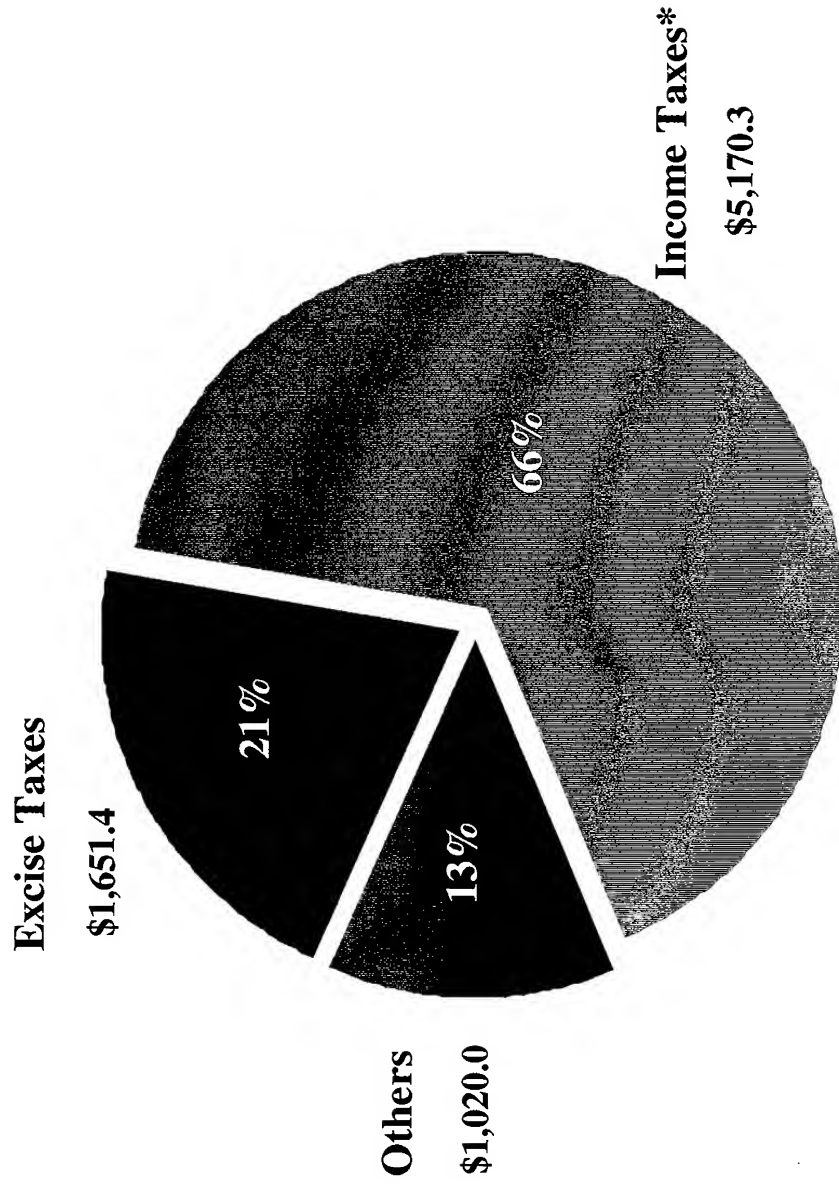
\*Includes proceeds of \$250 million line of credit obtained to replenish the income tax refund reserve.

Source: Puerto Rico Department of the Treasury

# COMMONWEALTH OF PUERTO RICO

## General Fund Net Revenue

For the fiscal year 2003  
(In millions)



Note: The net revenue presented above include the actual revenue and the operating transfers in from other funds presented in the combined statement of revenue and expenditures – budget and actual – budget basis.

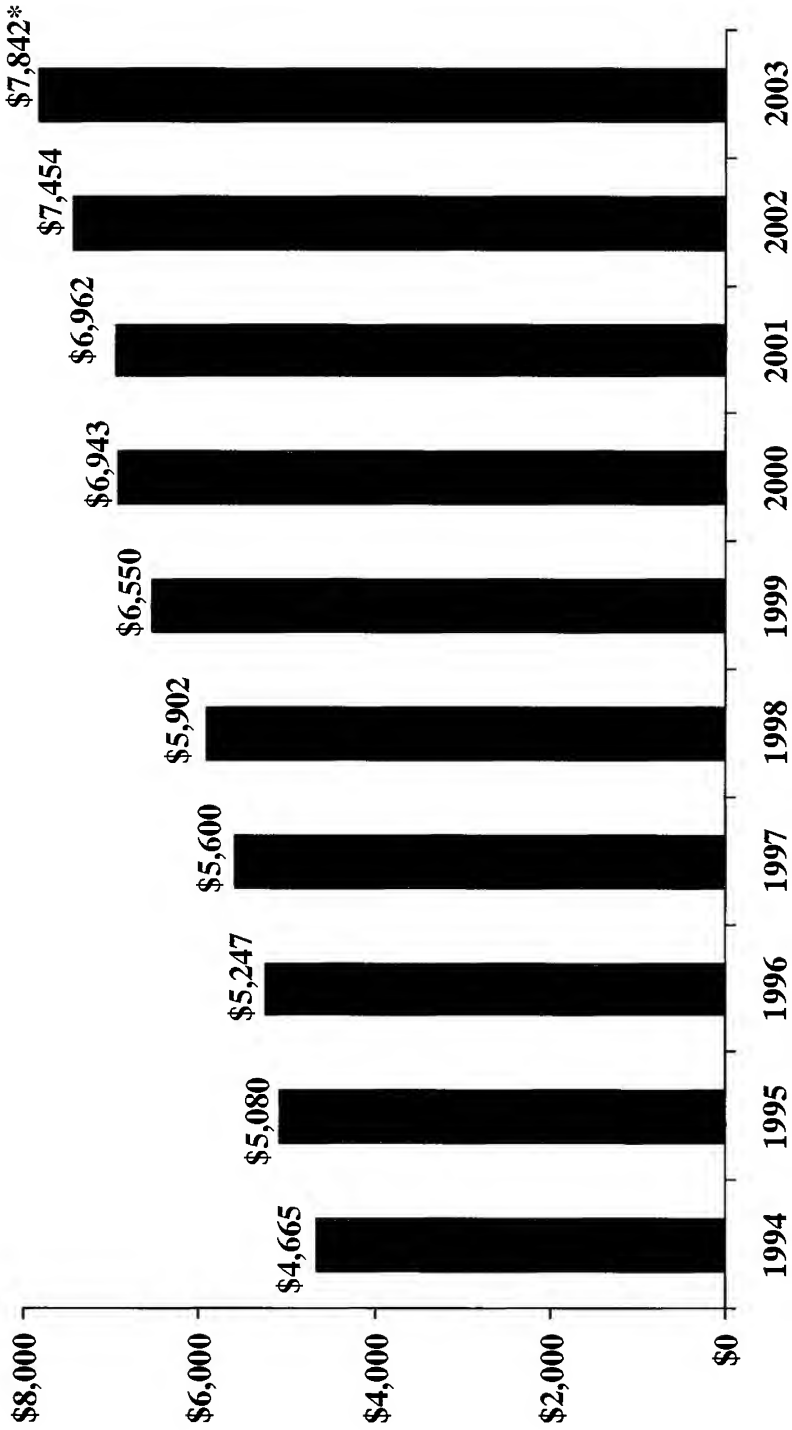
\* Includes proceeds of \$250 million line of credit obtained to replenish the income tax refund reserve.

Source: Puerto Rico Department of the Treasury

# COMMONWEALTH OF PUERTO RICO

## General Fund Net Revenue

For the last ten fiscal years  
(In millions)



Note: The net revenue presented above includes the actual revenue and the operating transfers in from other funds presented in the combined statement of revenue and expenditures – budget and actual – budget basis.

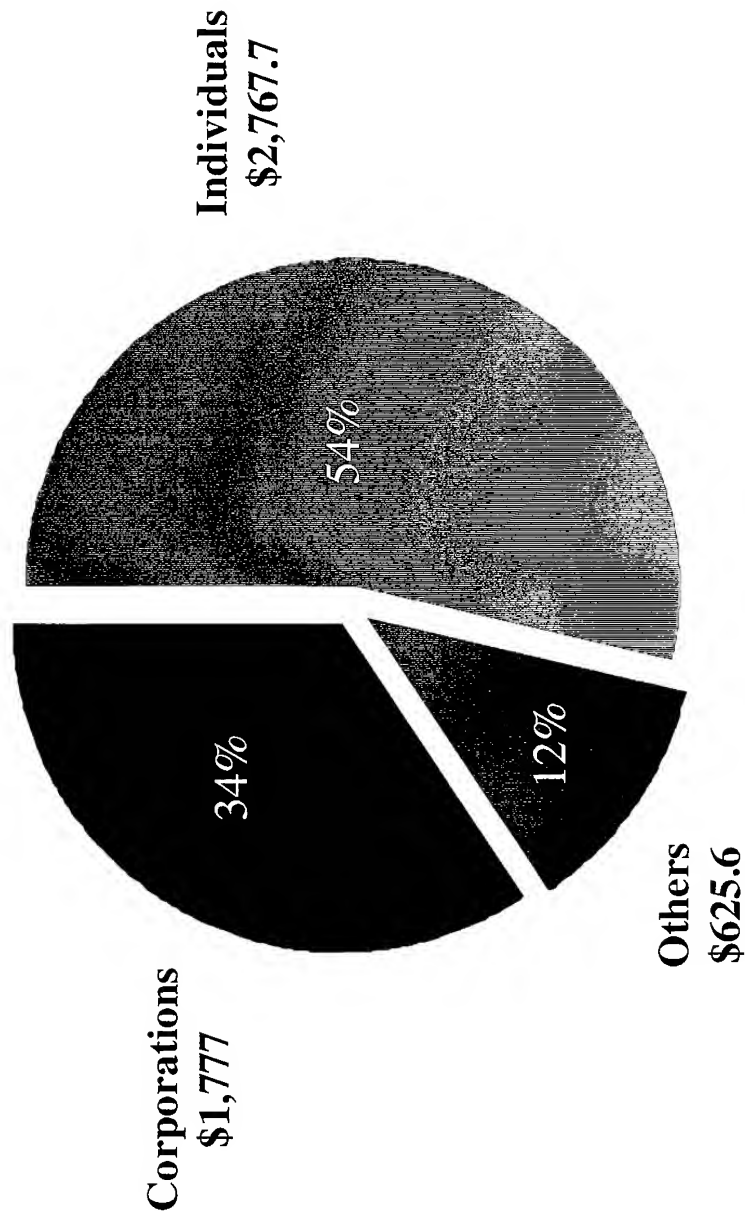
\*Includes proceeds of \$250 million line of credit obtained to replenish income tax refund reserve.

Source: Puerto Rico Department of the Treasury

# COMMONWEALTH OF PUERTO RICO

## Income Tax Receipts

For the fiscal year 2003  
(In millions)



Source: Puerto Rico Department of the Treasury



# COMMONWEALTH OF PUERTO RICO

## Gross Product

For the last ten fiscal years  
(In millions)

	2003 (p)	2002 (r)	2001 (r)	2000 (r)	1999 (r)	1998 (r)	1997 (r)	1996 (r)	1995 (r)	1994 (r)
Gross product - (current prices)	\$ 47,354	\$ 45,008	\$ 44,047	\$ 41,419	\$ 38,281	\$ 35,111	\$ 32,343	\$ 30,357	\$ 28,452	\$ 26,641
Real gross product - (2000 prices)	\$ 42,690	\$ 41,909	\$ 42,049	\$ 41,419	\$ 40,228	\$ 38,659	\$ 37,445	\$ 36,210	\$ 35,064	\$ 33,898
Increase (decrease) in real gross product (%)										
Puerto Rico	1.9	(0.3)	1.5	3.0	4.1	3.2	3.4	3.3	3.4	2.5
United States (1)	2.6	1.2	1.4	4.6	4.1	4.3	4.3	2.7	3.5	3.0

(r) Revised

(p) Preliminary

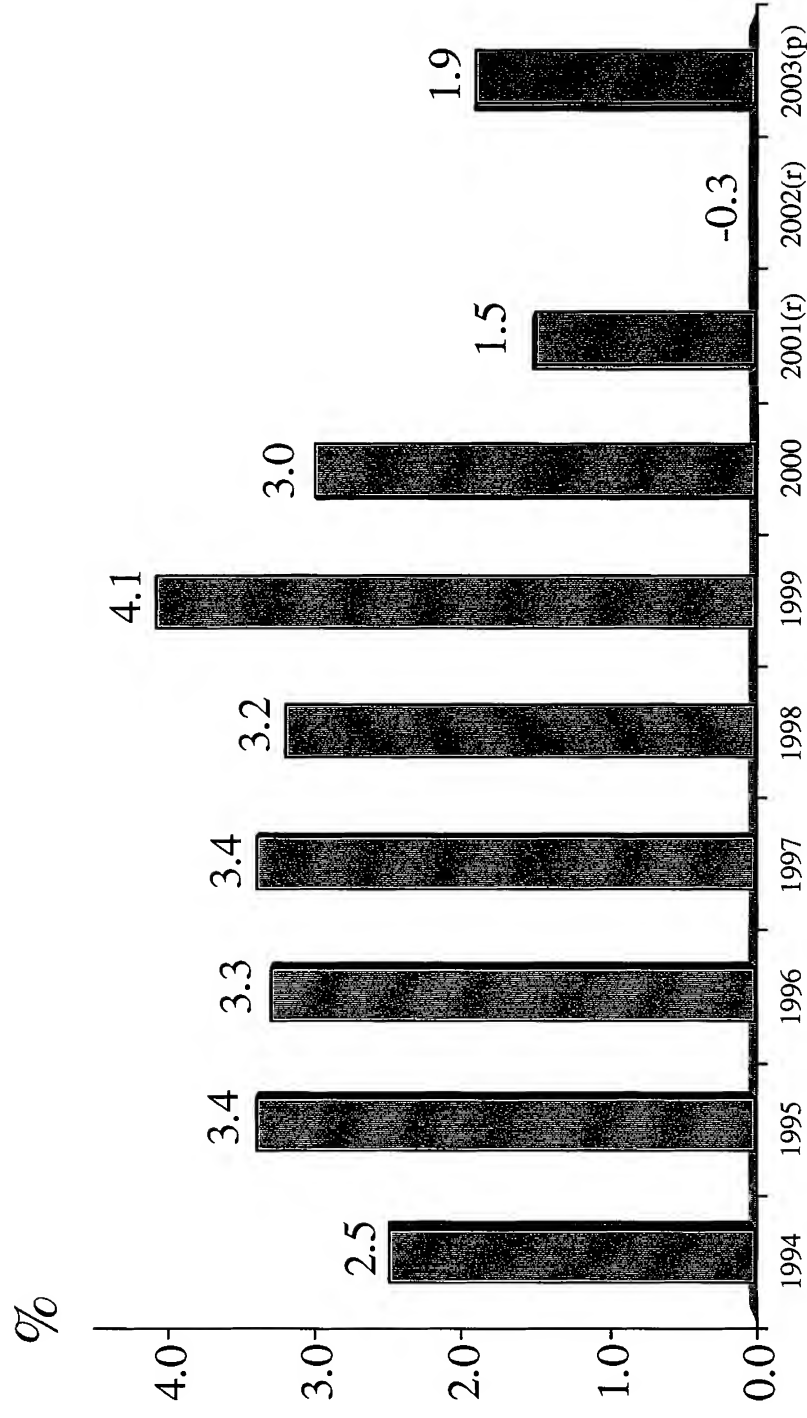
Source: Puerto Rico Planning Board and the Government Development Bank for Puerto Rico

(1) Based on 2000 Chained Method

# COMMONWEALTH OF PUERTO RICO

## Real Gross Product Growth

For the last ten fiscal years



(r) Revised  
(p) Preliminary

Source: Puerto Rico Planning Board

## COMMONWEALTH OF PUERTO RICO

### Employment and Unemployment

For the last ten fiscal years  
(In thousands)

Fiscal year	Labor force	Employed	Unemployed	Unemployment rate (%)
2003	1,378	1,211	167	12.1
2002	1,330	1,170	160	12.0
2001	1,293	1,158	135	10.5
2000	1,303	1,160	143	11.0
1999	1,310	1,147	163	12.5
1998	1,316	1,137	179	13.6
1997	1,298	1,128	170	13.1
1996	1,267	1,092	175	13.8
1995	1,219	1,051	168	13.8
1994	1,203	1,011	192	16.0

Source: Puerto Rico Department of Labor and Human Resources, Household Survey

**COMMONWEALTH OF PUERTO RICO**

**Average Employment by Sector**

**For the last ten fiscal years  
(In thousands)**

Sector	2003	2002	2001	2000	1999	1998	1997	1996	1995	1994
Agriculture	25	23	22	24	27	31	31	32	34	34
Manufacturing	136	139	159	159	159	161	161	167	172	166
Construction	83	86	85	85	78	69	64	59	57	54
Trade	257	240	242	239	229	236	228	218	211	201
Finance, insurance and real estates	45	43	41	42	43	40	37	39	36	33
Transportation, communications, and public utilities	56	62	56	55	59	59	59	61	59	55
Services	335	316	302	307	306	297	285	270	249	244
Government (1)	274	261	251	249	246	244	263	246	233	224
<b>Total</b>	<b>1,211</b>	<b>1,170</b>	<b>1,158</b>	<b>1,160</b>	<b>1,147</b>	<b>1,137</b>	<b>1,128</b>	<b>1,092</b>	<b>1,051</b>	<b>1,011</b>

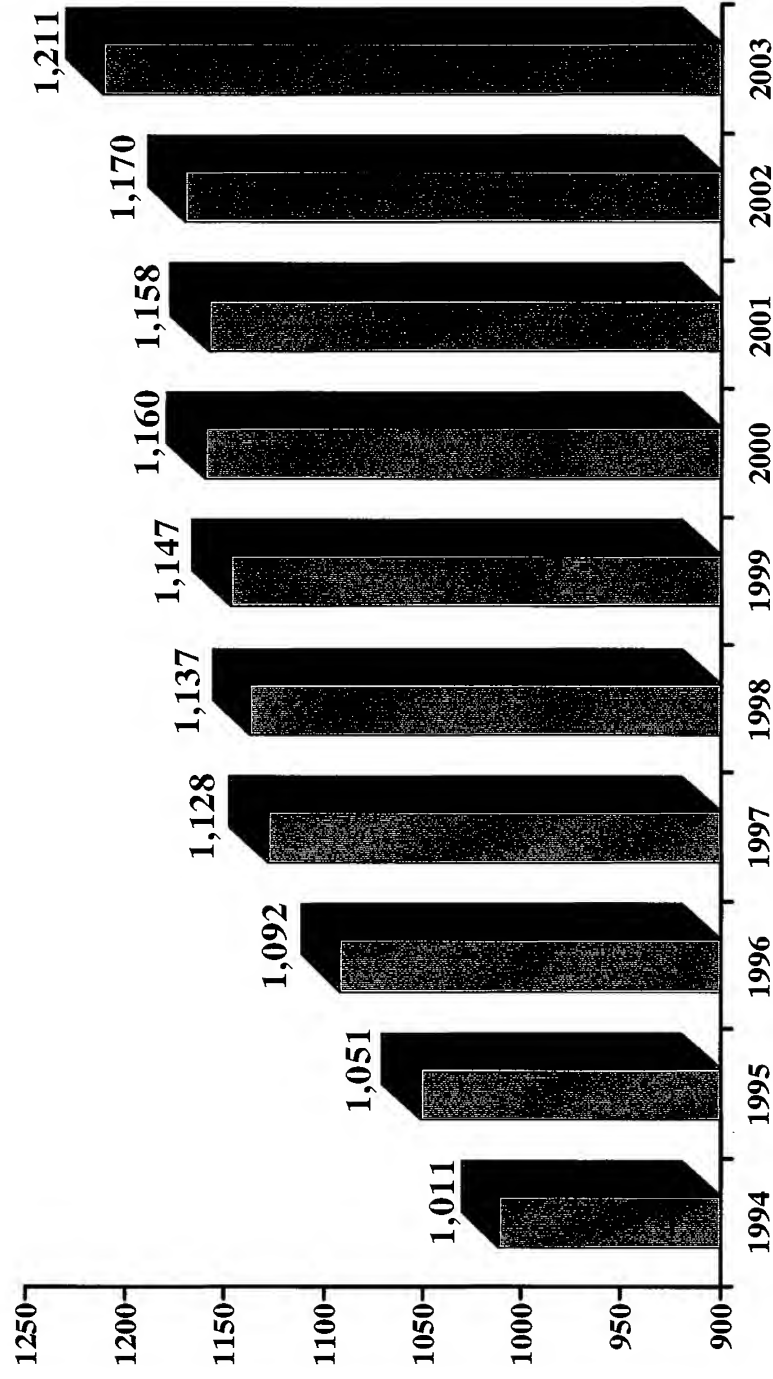
(1) Includes the Commonwealth, its municipalities, and federal government, and excludes public corporations.

Sources: Puerto Rico Department of Labor and Human Resources, Household Survey

# COMMONWEALTH OF PUERTO RICO

## Employment

For the last ten fiscal years  
(In thousands)



Source: Puerto Rico Department of Labor and Human Resources,  
Household Survey.

# COMMONWEALTH OF PUERTO RICO

## Tourism Indicators

For the last ten fiscal years

	2002(p)	2002(r)	2001	2000	1999	1998	1997	1996	1995	1994
All hotels and hostelry registration	1,969,862	1,821,274	1,836,377	1,674,092	1,637,620	1,570,683	1,461,567	1,400,815	1,302,387	1,177,571
Occupancy rates	64.9%	61.8%	66.7%	70.7%	71.9%	67.3%	69.8%	69.0%	68.0%	68.7%
Numbers of rooms	12,778	12,768	12,353	11,928	11,102	11,848	10,869	10,265	10,251	9,519
Visitors expenditures*	\$ 2,627	\$ 2,486	\$ 2,728	\$ 2,388	\$ 2,139	\$ 2,233	\$ 2,046	\$ 1,898	\$ 1,828	\$ 1,728

\*Amounts expressed in millions of dollars

(r) Revised

(p) Preliminary

Sources: Puerto Rico Tourism Company and Puerto Rico Planning Board

# COMMONWEALTH OF PUERTO RICO

## Government-wide Expenses by Function

For the last two fiscal years  
(In thousands)

Function:	2003	%	2002
General government	\$ 2,324,715	15.4%	\$ 1,429,265
Public safety	1,606,272	10.6%	1,883,061
Health	1,903,811	12.6%	1,990,852
Public housing and welfare	3,239,366	21.5%	2,803,742
Education	3,375,815	22.4%	3,477,373
Economic development	451,945	3.0%	632,083
Intergovernmental	466,762	3.1%	467,957
Interest and other	671,228	4.4%	646,120
<b>Total governmental funds</b>	<b>14,039,914</b>	<b>93.0%</b>	<b>13,330,453</b>
Lotteries	695,888	4.6%	603,768
Unemployment	343,243	2.3%	331,754
Other	22,385	0.1%	16,902
<b>Total business-type activities</b>	<b>1,061,516</b>	<b>7.0%</b>	<b>952,424</b>
<b>Total expenditures</b>			
<b>All governmental fund types</b>	<b>\$ 15,101,430</b>	<b>100.0%</b>	<b>\$ 14,282,877</b>

# COMMONWEALTH OF PUERTO RICO

## Government-wide Revenue by Source

For the last two fiscal years  
(In thousands)

Source:	2003	%	2002
<b>General revenue:</b>			
<b>Taxes:</b>			
Income	\$ 4,941,128	36.7%	4,446,570
Property	122,666	0.9%	102,554
Excise	1,894,729	14.1%	1,713,098
Other	3,055	0.0%	1,963
Revenue from global settlement agreement	101,849	0.8%	37,153
Unrestricted investments earnings	85,565	0.6%	127,395
Revenue from component units	111,752	0.8%	231,488
Grants and contributions not restricted to specific programs	103,423	0.8%	90,437
Payment from agency fund	—	0.0%	129,000
Special item	—	0.0%	123,785
Other	91,715	0.7%	472,642
<b>Total</b>	<b>7,455,882</b>	<b>55.4%</b>	<b>7,476,085</b>
<b>Program revenue:</b>			
<b>Governmental activities:</b>			
Charges for services	757,116	5.6%	535,423
Operating grants and contributions	3,830,639	28.5%	3,400,729
Capital grants and contributions	173,644	1.3%	187,512
<b>Total</b>	<b>4,761,399</b>	<b>35.4%</b>	<b>4,123,664</b>
<b>Business activities:</b>			
Charges for services	1,132,285	8.4%	1,021,070
Operating grants and contributions	97,033	0.7%	26,509
<b>Total</b>	<b>1,229,318</b>	<b>9.1%</b>	<b>1,047,579</b>
<b>Total revenue –</b>			
<b>Governmental and business-type activities</b>	<b>\$ 13,446,599</b>	<b>100.0%</b>	<b>\$ 12,647,328</b>